

## Foreign Investments and Socialist Enterprise in Slovenia (Yugoslavia): The Case of the Kolektor Company

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In this article, I examine foreign investment in the socialist enterprise in the former Yugoslavia based on the case study of Kolektor in the context of the liberalized communist social and economic order. Foreign investments were allowed in the form of joint ventures. I present these investments from the viewpoint of economic reforms, the concept of socialist enterprise, and the concept of economic development, which enabled foreign investments and shaped regulation and the structure of foreign investments in Yugoslavia. The history of the case of Kolektor began at a time when Slovenia still belonged to the former Yugoslavia, which was arguably a liberalized type of communist economic system. This was during the Cold War, when both Europe and the rest of the world were divided essentially along the lines of the communist east and the capitalist west. The Kolektor Company was established in 1963 as a state socialist enterprise for the manufacture of the rotary electrical switches known as commutators. From the outset, the company tried to establish international cooperation to acquire modern technology. In 1968, it reached an agreement with the West German Company Kautt & Bux, which at the time was the technological and market leader in the production of commutators. Kautt & Bux invested in Kolektor and became an owner of 49 percent of the company. The investment proved very profitable for both partners. The Slovenian side got access to modern technology and expertise, and the German side got additional production facilities, skilled workers, and low-cost production, which increased its competitiveness on international markets.

Keywords: Yugoslavia, Slovenia, communism, commutator economic reforms, socialist enterprise, joint ventures

### *Introduction*

In this article, I examine foreign investments in Yugoslav companies during the communist period. Yugoslavia was among the first communist countries to allow foreign investments in the form of joint ventures in 1967. Later, it was followed by other communist countries. Yugoslavia attracted a larger volume of foreign investments than all other communist countries put together. It differed from the other Eastern Bloc countries because its economic and political system was

decentralized, the state was better integrated into the global economy, its foreign economic relations were liberalized, and individual companies were responsible for their own success. This paved the way for foreign investments once they were allowed. The system of self-management was introduced with reforms in the early 1950s. It prospered thanks to a significant level of decentralized decision-making at the political and economic level. In the middle of the 1960s, it was decided that foreign investments in Yugoslav companies should be allowed, together with the integration into the international division of labor. The decision was strategic and pragmatic. In close cooperation with foreign partners, domestic companies would get access to modern technologies and management know-how, and they thus would be better able to penetrate Western markets. Also, foreign investments were cheaper than the importation of foreign capital through state borrowing. After that, the idea of attempting to attract foreign investment persisted in the Yugoslav territory until the dissolution of the state in 1991. Over the course of a period of twenty years, regulations would keep changing, becoming increasingly favorable to foreign investment, depending on the political circumstances.

The article is divided into six shorter sections. The first section summarizes the economic reforms and development periods during the existence of communist Yugoslavia. The second section analyses the distinctive characteristics of Yugoslav companies, which must be taken into consideration if one seeks to understand the positions of foreign investors. The third section traces the institutionalization of foreign investments. The fourth focuses on the regulation of foreign investments with emphasis on the essential aspects of regulation and changes over time. The fifth section examines the scope of foreign investments in view of the sectoral structure, regional distribution, and origins of foreign investors. A detailed case study of foreign investment follows in the sixth section, specifically the Western German Kautt & Bux company's joint venture with Kolektor from Slovenia. The case study illustrates the pattern of investment in a Yugoslav company and of cohabitation between a foreign partner and a self-management company. This company's experiences, however, were not typical of the practice of foreign investment into Yugoslav companies. Its long-term success makes it an exception, as most of the joint ventures were of a comparatively short duration and were of limited expansion and innovation. Kolektor, rather, offers a good example of what the Yugoslav authorities envisioned and hoped for when they decided to allow foreign investors to partner with domestic enterprises.

## *Economic Models*

Economic development in Yugoslavia can be divided into four periods, each of which saw the emergence of a distinctive economic model. The first one lasted from 1947 to 1951. This period saw the rise of a centrally planned economy. In other words, it was the period in which administrative planning was implemented according to the Soviet example. The top priority was to develop heavy industry even if it meant neglecting other sectors, including sectors which had a direct impact on people's living standards. In the second period, central administrative planning was abolished (1952–1965). The plan became a mere orientation concerning how the economy was supposed to develop. Furthermore, it became polycentric, as the individual republics attained the right to specify the priorities when it came to their economic development. In the context of the goals specified in such a manner, the companies would supposedly pursue their interests. Partial competition among companies was enabled. Companies were allowed to establish horizontal connections, i.e., communicate among themselves according to their business interests. Thus, hierarchic communication with the ministries in the framework of the centrally planned company activities was abolished. With reforms, decision-making was divided between the political and economic level. Companies became responsible for their own success, and their leaderships could make business decisions autonomously. The new economic model emphasized the development of the consumer goods industry and intensive rather than extensive development, i.e., productivity growth, business efficiency, and the liberalization of international trade. The third period (1965–1975) was called the period of “market socialism.” It saw the use of so-called indicative planning. Companies set their own business objectives in line with the national economic development plan. The focus of economic policy was on boosting consumer spending and income growth. The strengthening of the secondary and tertiary sectors, the integration of Yugoslavia into the international economic space, and the international division of labor were also emphasized. The intention was to strengthen the functioning of the market and the productivity and efficiency of the economy, to increase the level of general education, and to enhance the role of business research and development, either independently of or in connection with the academic sphere. The fourth and last period (1976–1991) was characterized by the consolidation of “workers’ self-management.” A turning point came when the society and the economy were reorganized according to the principles of the so-called “contractual economy,”

which was supposed to strengthen the influence of workers (through self-management) in the management of economic entities. From the strategic point of view, the country changed its model and focused on the promotion of basic industries, energy, and raw materials. Attention was also paid to export growth, the reduction of the deficit in the balance of payments, efficient energy use, higher productivity, and closing the regional and economic gaps. The general decentralization of decision-making altered the nature of social planning. The planned goals became a synthesis of the planning by different actors, including companies, associations, and public authorities. Due to measures which were taken to further decentralization, which in turn diminished the power of the state authorities (especially the federal ones), the role of the renamed Communist Party became very important. With its cells in all of the social and economic units, the Communist Party, the League of Communists of Yugoslavia (LCY), became an informal integrating element of a fragmented society and economy.<sup>1</sup>

### *Yugoslav Companies*

Foreign investments were also determined by the structure and concept of socialist enterprises in Yugoslavia, where there was a system of ownership that was unique in the Socialist Bloc. With the abandonment of the centrally planned economy and the introduction of “workers’ self-management,” the concept of state ownership and hierarchical management of socialist enterprises was abolished as well. In the context of the reforms, companies were becoming responsible for their own success. They were able to establish connections and engage in cooperative business endeavors according to their own interests and the demands of their activities. The transfer of responsibilities to companies took place in the context of the general decentralization of the state. At the same time, the transfer to lower units also meant a change in the ownership concept. The concept of state ownership was replaced by that of “social ownership.” According to this concept, the company was the property of society, i.e., of the entire population. Meanwhile, the workers were intended to run the company. The concept of social property was linked to the concept of “workers’ self-management.” This meant that company employees had the right to manage the

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1 Ramnat, “Yugoslavia: Self-Management”; Prinčič, “Tuje naložbe”; Woodward, *Socialist Unemployment*, 165–90; Bičanić, *Economic Policy*, 192–210; Flakierski, *The Economic System*; Dyker, *Yugoslavia – Socialism, Development, Debt*, 19–90.

company, determine its activities, production volumes, sales prices, marketing strategies, investments, and the use of profits.<sup>2</sup>

In Yugoslavia, a company could be set up by a municipality, a republic, the federation, another company, a bank, or even a group of citizens. New companies could also be created by merging or splitting up existing enterprises. The founder was obliged to provide the necessary capital. Companies were autonomous in determining their business policies. The power in the company hinged on the working community. With their employment in the company, all workers acquired the right to co-manage the company. The working community would elect the highest management body in the company: the “workers’ council.” The workers’ council decided on all business strategies and implementation orientations. It also appointed the company’s management, board of directors, and the director. Board members were accountable to the workers’ council. The director was appointed by the workers’ council. The decision was formally based on the council’s public call for candidates, but the local party leadership initially made the choice. The period of tenure was four years, and there were no limitations on the number of terms. The director managed and administered the company on behalf of and by the authority of the workers’ council. In his work, he had to pursue the interests of the “working community,” to which he was ultimately accountable. The director had the right and obligation to participate in the workers’ council meetings, but he or she was not supposed to play a decisive role. The question of the realistic distribution of power, responsibility, and authority in Yugoslav companies was crucial for foreign investment decisions. Individual directors would successfully lead companies through the strength of their personalities and persuasive abilities. However, the real power of the workers’ councils also had to be taken into account.<sup>3</sup>

The notion of workers’ self-management was not merely a matter of abstract conceptual thinking or disingenuous rhetoric. It had to be taken seriously in case of every intention of foreign investment, and the investments had to be negotiated with the company itself or with its management. On the other hand, Yugoslav companies were obliged to secure the consent of the authorities and political bodies. Another important issue also arises in connection with the roles of political bodies: that of political intervention in companies. Foreign investors needed to consider this possibility as well. As the reforms weakened

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2 Conner, “Joint Ventures in Yugoslavia,” 46.

3 Milutinovich et al., “Investment in Yugoslavia,” 53.

the influence of the central authorities in companies, the influence of the party authorities within the given republic and district survived. The LCY had cells in every social organization, including companies. The political line would thus control the company and supervise the decision-making mechanisms and company management. As party members, the directors had a twofold responsibility. On the one hand, they were accountable to the employees, i.e., to the “workers’ council,” but they were also accountable (as noted above) to the local party leadership.<sup>4</sup> In practice, this meant that there were formal and informal levels of decision-making which were sometimes complementary and sometimes conflicting. Meanwhile, the LCY had a monopoly on personnel policy. Decentralization also implied a transfer of social power. Corporate self-responsibility also meant that the social power of company managements grew in strength. The control exerted through the local Communist Party authorities at the company and municipal level was intended precisely to regulate this power. This was necessary to ensure that companies would pursue the overall social objectives rather than just their own aims. However, in this manner, the companies’ “self-management” and self-responsibility for their own economic success was systemically denied. Company leaderships would struggle to balance their political and economic performances, with the former often taking precedence. This dilemma was identified at the time by domestic critics, who also questioned the concept of market socialism.<sup>5</sup>

### *The Decision to Accept and Encourage Foreign Investment*

Yugoslavia was the first socialist country to allow foreign investment in its economy. Hungary, Poland, Romania, and Bulgaria followed later.<sup>6</sup> Due to the nature of the system, the investments could only take the form of joint ventures. The 1960s were an important period in the economic history of Yugoslavia (and Slovenia). They bore witness to a significant attempt to change the economic and social landscape. Economic reforms were implemented to make the economy more efficient, increase business incomes, and make the economy more competitive in foreign markets. Naturally, everything was done within the framework of the communist ideology, which meant that change was desirable, but only to the point where it did not threaten the existing fundamental postulates

4 Prinčič, “Direktorski položaj.”

5 Bučar, *Podjetje in družba*, 109–20.

6 Bozescu, “Joint-Ventures in Eastern Europe.”

of the communist political, social, and economic order. Thus, in the process of phasing out the centrally planned model, the state started to shift some of the responsibility for economic success to businesses and local communities. It only allowed the market to function, but only within limits set by the state, and it refused to give up the mechanisms with which it controlled the economy. The state also promoted the integration of companies into the international environment. In principle, it supported integration into the international trade flows and the international division of labor. The internal and external trade regimes were gradually liberalized, and some measures were even taken to attract foreign capital.<sup>7</sup>

Foreign investment was one of the major development issues in this process. At the time, after the country's accession to the General Agreement on Trade and Tariffs (GATT), following the adoption of the Great Economic Reform (1965), the Yugoslav authorities wanted to integrate the country into the international division of labor. The 1965 reform was one of the most comprehensive and profound of the Yugoslav economic reforms. After these reforms were adopted, the concept of market socialism was consolidated. At the time, it was clear that integration into the international division of labor also meant opening up the country to foreign investment. For a short time, a view prevailed according to which it was socially cheaper to allow foreign capital to enter domestic companies than to build economic development solely on foreign loans.<sup>8</sup> However, the price of capital was not the only factor. The expectation was that domestic companies would thereby gain swifter access to modern technologies and, by leaning on foreign partners, enter foreign markets.<sup>9</sup> It was also expected that the "workers' self-management" would become stronger, the general economy and individual enterprises would become more efficient and profitable, and the pace of industrialization would accelerate. Furthermore, the balance of payments was also supposed to improve, as foreign investment would boost exports of higher-value products and help the country address its capital shortage. The issue of unemployment was pressing. The decision was adopted in a context of very high levels of recognized unemployment and increasing economic emigration to Western European countries. It was hoped that foreign investments would allow the country to create jobs more quickly.<sup>10</sup>

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7 Prinčič, *V začaranem krogu*, 117–32.

8 Gnjatović, *Uloga inostranih sredstava*, 90–93.

9 Prinčič, *V začaranem krogu*, 117–32; Prinčič, "Tuje naložbe."

10 Chittle, "Direct Foreign Investment," 771–73.

### *Regulation of Foreign Investments*

Foreign investment was regulated by specific legislation which was adopted in various stages. At the initial stage, acts which paved the way for joint ventures were adopted. In the subsequent stages, more detailed regulation of the relationships followed. The process started in 1967, when an act was adopted to tax the profits of foreign companies that invested in Yugoslav companies. A second act limited the foreign investor's share. The domestic company had to hold the majority in the joint venture (at least 51 percent). Foreign investment was not allowed in banking, the insurance industry, domestic transport, trade, and public utility services. The domestic and foreign partner had to conclude a joint venture agreement, define the purpose of the agreement, and determine the mutual relations in terms of capital, management, cooperation, operations in domestic and foreign markets, and, of course, the division of profits.<sup>11</sup> The domestic company had to obtain the informal consent of the republic's authorities even to enter the initial negotiations. After the conclusion of the agreement, it had to be sent for approval and entry in a special register of such companies at the Federal Ministry of Economy in Belgrade. The foreign partner was guaranteed certain rights under the law: the right to retain ownership of its capital contribution and to sell it, the right to a proportionate share of the profits, the right to comanage the company, and the right to access all documentation. It was also very important that the foreign partner had the right to repatriate the majority of its share of the profits. In summary, foreign investors were allowed to manage the company and participate in it based on ownership (investment). Rights went hand in hand with duties. Thus, the foreign partner had to reinvest at least one fifth (20 percent) of the profits in the domestic company or invest them in a Yugoslav bank at the usual interest rate. The foreign partner also had to pay the required taxes: a profit tax of 35 percent, which was supposed to be a more favorable tax rate than in Western European countries, where most of the potential interest in investing in Yugoslav companies was expected to be found.<sup>12</sup>

The 1970s were a decade of contradictions. In 1971, although the requirement to reinvest part of profits was abolished, the foreign investor could repatriate only one-third of the income earned by exports after having paid the relevant taxes. The individual republics were allowed to set their own tax rates on foreign

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11 Sukijanović and Vujačić, *Industrial Cooperation*, 22–38.

12 *Investiranje stranog kapitala*.

investments. In 1973, long-term investments and the joint and several liability of Yugoslav companies in joint ventures with foreign investors were regulated in more discouraging detail. In June 1976, conditions for foreign investments were tightened. Only foreign investment aimed at exports for foreign markets would be approved. Contracts needed to be more precise. The volume of exports and the currencies had to be specified for foreign investors to receive their profits. The rights of joint management bodies were also limited in the sense that they were not allowed to interfere with the “self-managing” structure of companies. The responsibility to determine business policy was transferred to work councils. This limited the foreign investor’s right to manage the company. These repeated changes limited growth in foreign investment.

The legislative changes of April 1978 were again more favorable to foreign investment, as special protections were granted to foreign investors. This time, the legislature put foreign investors on an equal footing with domestic companies in terms of the right to manage. The rights of the company’s joint management board were laid out in detail. In addition, foreign investment in banking was allowed, which was to be regulated by a special act. Foreign investment in the insurance industry, trade, and public utility services remained prohibited. A provision that allowed foreign investors to repatriate half of their export profits was important for them. The next step was taken in 1984, when ownership restrictions were lifted. Foreign investors could now also become majority owners. The last change dates to 1988, when a new foreign investment act completely freed up foreign investment. Prohibitions in the military industry, rail and air transport, telecommunications, the insurance industry, and media remained in place. The act put foreign investors on an equal footing with domestic companies in terms of tax reliefs and government incentives. The foreign investor acquired all management rights and the right to transfer all profits, and collective agreements would be concluded with the employees.<sup>13</sup>

### *Foreign Investments in Yugoslavia*

The Yugoslav joint ventures policy attracted the attention of the international business, academic, and political public. The number of articles and expert analyses on the subject was considerable. This had an impact on the flow of capital into Yugoslavia. Yugoslavia succeeded in attracting investments from the

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13 Prinčič, “Tuje naložbe,” 112–19; Artisien and Buckley, “Joint Ventures in Yugoslavia,” 117–20.

most technologically and economically advanced countries. The data from 1980, compiled by the OECD, indicate that the volume of foreign investment was gradually increasing.<sup>14</sup> Among the industrial sectors, metalworking, the chemical industry, and transport equipment manufacturing attracted the most investment. Despite the constantly changing regulatory measures concerning joint ventures, the political-ideological prejudices in the country, and the actual constraints of the political and economic system, the volume of foreign investment should be deemed only a limited success, since its total value remained a small share of capital in all sectors except metal production (see Table 1). The interest from foreign private Western companies was still considerable, especially those that had already established cooperation with Yugoslav companies. The Western companies' motives for investing in Yugoslav companies varied and, above all, included the low price of labor and the tax advantages, which allowed for the acquisition of the Yugoslav market, sales through Yugoslav companies to other communist countries, and competitive exports to Western markets due to the low price of labor. As a rule, investments would be proposed by Yugoslav companies.<sup>15</sup> The main motivation of foreign companies was, therefore, further growth, profitability, and export opportunities to third markets. Foreign companies that strived to understand the Yugoslav ideological-political reality were successful at investing. A survey of a sample of Western companies in Yugoslavia showed that

Table 1. Foreign investments by economic sector, 1968–1980

Sector	Number of contracts	Total investments (millions of dinars)	Share of capital
Food, Drinks, and Tobacco	17	2,577	5.5 %
Chemicals and Allied Industries	27	5,843	12.5 %
Industries in Which Metals Were Used	17	2,269	4.8 %
Production of Metals	12	22,218	47.8 %
Wood and Paper Industry	8	3,094	6.7 %
Transport Equipment	17	5,860	12.6 %
Electrical Engineering	14	1,395	2.9 %
Rubber Industry	8	2,178	4.7 %
Other Industries and Activities	44	1,137	2.5 %

*Source:* Artisien and Buckley, "Joint Ventures in Yugoslavia," 116.

14 Artisien and Buckley, "Joint Ventures in Yugoslavia," 114–17.

15 Patton and Do, "Joint Ventures in Yugoslavia," 53.

investments in Yugoslav companies met their expectations. Foreign companies would follow several investment goals. The relatively lower return on investment was compensated for by the increase in exports to other communist countries and the conquest of the Yugoslav market.<sup>16</sup>

While foreign investors were evenly distributed, most came from countries that were also Yugoslavia's largest foreign trade partners. The main players were companies from the contemporaneous European Economic Community. Unsurprisingly, Germany and Italy were in the first place (see Table 2). They were followed closely by companies from the United States of America, though only in terms of the number of contracts concluded. However, the United States was the top investor by far in terms of capital invested due to their heavy investment in the oil refining industry.

Table 2. Origin of foreign investors in Yugoslav enterprises, 1968–1980

Countries of origin	Number of contracts	Foreign capital invested (millions of dinars)	Share of total foreign capital
USA	30	3,368.0	32.8 %
UK	12	1,777.8	17.3 %
Switzerland	19	1,637.1	16.0 %
West Germany	52	1,123.0	11.0 %
Italy	31	937.6	9.1 %
France	11	290.0	2.8 %
Austria	7	254.1	2.5 %
Sweden	6	223.3	2.2 %
Luxembourg	4	126.0	1.2 %
Belgium	6	124.4	1.2 %
Netherlands	3	75.6	0.7 %
Others	17	402.2	3.2 %

*Source:* Artisien and Buckley, "Joint Ventures in Yugoslavia," 115.

While foreign investments in Yugoslav companies were territorially dispersed throughout the country, they were also regionally concentrated. The idea of the Yugoslav economic development planning that foreign investment would contribute to the more rapid development of the underdeveloped republics was not realized. Most joint ventures were secured by companies from the developed

<sup>16</sup> Lamers, *Joint Ventures Between Yugoslav and Foreign Enterprises*, 205–16; Artisien and Buckley, "Joint Ventures in Yugoslavia," 120–32.

regions of Slovenia, Croatia, and Serbia (see Table 3). As the legislation allowed it, a kind of “competition” emerged to attract joint ventures. The underdeveloped republics offered lower tax rates to attract a higher share of foreign investments. Montenegro, Vojvodina, and Kosovo set a tax rate of 10 percent. The Kosovo authorities offered an even more reduced rate of only 5 percent for investments in Kosovo’s underdeveloped municipalities. Serbia and Macedonia set tax rates of 15 percent and 14 percent, respectively. In Serbia, any foreign investor could benefit from a half tax rate if they invested in economically less developed areas. Slovenia and Bosnia and Herzegovina set their tax rates at 20 percent. Croatia taxed foreign investors more, at 35 percent. However, it also recognized reduced rates, for example, in the case of investments in tourism activities, the rate was only 5 percent for the first five years and 20 percent thereafter.<sup>17</sup> However, through tax policy alone, the underdeveloped republics could not make up for the advantages of the developed republics, which offered a better educated and experienced workforce, better infrastructure, more efficient companies, and better integration into the international economic space.

Table 3. Regional distribution of foreign investments in Yugoslavia 1968–1980

Location	Number of joint ventures	In millions of dinars	Share
Serbia proper	41	2,589	30.9 %
Croatia	34	2,585	30.9 %
Bosnia-Herzegovina	29	1,186	14.2 %
Slovenia	43	1,026	12.4 %
Vojvodina	9	470	5.6 %
Macedonia	6	184	2.2 %
Kosovo	3	180	2.2 %
Montenegro	2	134	1.6 %

*Source:* Prinčič, “Tuja naložbe,” 116.

In the individual republics, special bodies were established to attract foreign investments. In Slovenia, these bodies were a part of the Chamber of Commerce and the state administration. The Chamber of Commerce established a Foreign Capital Investment Commission to provide legal and economic information to domestic and foreign companies and to assist them in making foreign investments. The same role was performed by the Work Group on Foreign Investments of

<sup>17</sup> Artisien, *Joint Ventures in Yugoslav Industry*, 115.

the Ministry of Economic Cooperation with Foreign Countries of the Socialist Republic of Slovenia.<sup>18</sup> At the international level, a special organization called the International Investment Corporation for Yugoslavia (IICY) was established to provide support for interested foreign companies. The project idea was developed in the Yugoslav banking circles to facilitate and purposely promote foreign investments in Yugoslav companies. In November 1968, a group of Yugoslav bankers, in cooperation with the International Finance Corporation of the World Bank Group (IFC), initiated consultations about the new institution. The response among Western bankers was sufficient for a decision to set up an institution aimed at providing assistance for private enterprises regarding their cooperation with Yugoslav companies. It would help them find business partners and raise the necessary capital in the form of loans or venture capital. The primary objective was to bring modern production techniques and management know-how to Yugoslavia. The IICY became operational in December 1969. It was based in London, Europe's largest financial center, but registered in Luxembourg for tax reasons. The founding capital in the amount of 12 million US dollars was contributed by 12 Yugoslav and 39 foreign banks, with the assistance of the International Finance Corporation. The founding banks described the new institution as a "pioneering type of investment company, through which private business will invest in joint industrial, agricultural and tourism and other services ventures in Yugoslavia." The largest shareholders included Yugoslav banks and banks from Austria, Germany, Switzerland, France, Italy, and the Netherlands, i.e., from the countries with which Yugoslavia had already developed economic cooperation. However, financial institutions from the USA, UK, Sweden, Japan, and Kuwait were among the shareholders as well. In the early years, the IICY played an important role in attracting foreign capital to Yugoslavia. By 1973, it had participated in 22 percent of the total investments and provided capital support for these investments. It also invested in its own name, partly in the form of loans and partly in the form of risk capital. Its representatives ensured that investments were balanced regionally and by sector. As the Yugoslav banks and their international activities expanded, the IICY's importance gradually diminished, as had been expected would happen when it was founded.<sup>19</sup>

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18 Prinčič, "Tuja naložbe," 117.

19 Lamers, *Joint Ventures Between Yugoslav and Foreign Enterprises*, 216–19; Patton and Do, "Joint Ventures in Yugoslavia," 54.

*“We Worked in Socialism, but We Need to Act and Think as if We Were in Capitalism.”<sup>20</sup> The Case of the Joint Venture between Kolektor and Kautt & Bux*

The Kolektor Company was established in 1963 as a state socialist enterprise for the production of commutators. From the outset, they tried to establish international cooperation in order to acquire modern technology. In 1968, when for the first time the joint ventures were allowed, Kolektor made an agreement with the West German Company Kautt & Bux, which at the time was the technological and market leader in the production of commutators. Kautt & Bux invested in Kolektor and became the owner of 49 percent of the company. The investment proved very profitable, as both partners benefited. The Slovene side got access to modern technology and expertise, and the German side got additional production facilities, skilled workers, and low-cost production, which increased its competitiveness on international markets. The German side also got the exclusive right to handle marketing. Kolektor was only allowed to sell products under its own brand in the communist part of Europe. The investments in development and technology were always very high, and both partners were obliged to make them. As a foreign partner, Kautt & Bux had to invest at least 20 percent of its profit in order to be allowed to export the rest of its profits. Both partners also made a commitment to decide jointly on reinvesting the profits and on additional investment above the legally set limit of 20 percent. Kautt & Bux regularly reinvested the generated profits. The repatriation of profits represented a mere 2 percent of the profit per year.

The main threat to cooperation with foreign partners was the system of management of Slovenian and Yugoslav enterprises. It was based on the ideology of socialist self-management, according to which all decisions on business processes were to be entrusted to the “workers council.” In Kolektor, they had to deal with this obligation on a daily basis. The company tried to be flexible. On the one hand, they insisted on contractual provisions, but on the other, they strove for balance with the Yugoslav provisions on self-management. Fortunately, Kautt & Bux was equally pragmatic. Two parallel “mind” structures were thus pragmatically established in Kolektor. They differed completely in their origin, backgrounds, and purposes. The “communist” and “capitalist” structures and methods of management intertwined in the company’s operations. The latter structure eventually prevailed. Jožica Velikajne, a long-standing associate

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20 Jožica Velikajne, a former employee of Kolektor, on the joint venture with Kautt & Bux.

of the company, described the split personality of the company: “Half of the time, we lived in socialism and the other half in capitalism.” But a pragmatic solution was found which was respected by both sides and which enabled long-lasting cooperation. With the entering of German investors, Kolektor began to undergo a process of deep economic, social, and cultural changes. Kolektor was partly excluded from the local environment. Kolektor’s management structure was different. It was led by two codirectors, one from Germany and one from Slovenia. Decisions could be made only with the agreement of both sides. Kolektor as a company was faced with an urgent need to adapt to western, namely German business standards and habits, well also dealing with the characteristics of the local communist environment.

Kautt & Bux assured itself control over management of the company and thus protected its interests, but this indirectly brought it into a “systemically built-in” conflict with the self-management system. This is why it was also ready to give certain concessions to the Slovene factory. In one of the provisions, Kolektor received an assurance that Kautt & Bux would guarantee each year a minimum volume of sales of Kolektor commutators on foreign markets. This was a great achievement for the factory, as it made a much-desired expansion possible. They could thus use the revenues from exports to finance the modernization and expansion of production capacities and the import of special tools and indispensable semi-finished parts. Both partners also made a commitment to decide jointly on reinvesting the profits and on additional investment above the legally set limit of 20 percent.

In line with the existing legislation, the contract laid down that the company would be managed by a joint management committee with a full mandate to run the company. Yet the self-management organization of the company had to remain intact. But once again, Kautt & Bux got a concession here. At its request, a provision was added to the contract according to which “the supreme self-management body,” i.e., the “workers’ council,” had to respect all contractual provisions and all decisions taken by the joint management committee. In this manner, the German partner assured itself in advance of the protection of its interests.

Another part of the process of establishing cooperation between the two companies and entering into a joint venture was a financial check-up of the company, which took place in November 1968. The German partner was interested in the structure and method of Yugoslav bookkeeping and accounting, including its everyday practices and categories. It wanted to check the credibility

of the financial statements of the Kolektor company. It sent to Kolektor a group of three accounting and tax experts. Their report confirmed the credibility of the financial statements. They even concluded that the bookkeeping and accounting at Kolektor was very good and precise in every detail. The auditors, however, noted certain terminological differences stemming from the Yugoslav system and accounting standards. They recommended standardizing the terms or specifying clearer definitions of individual terms so that their meanings would not be lost in translation. They were extremely satisfied with the financial control exerted by the authorized state services, in particular the audit service of the central bank. They even found a good feature in the management structure of Yugoslav enterprises. They believed that the controlling authority of workers' councils was a good solution, as such internal control largely prevented the possibility of personal profiteering. They eventually reminded the accounting service of the obligation to send quarterly financial statements to Stuttgart. Thus, the accounting service was subject to additional control. But it was very important that the representatives of Kautt & Bux trusted the accounting service and did not question the credibility of its reports.

Kolektor was one of the first cases of an investment by a Western European partner in a self-managed socialist company in Slovenia and even in Yugoslavia. There were, understandably, many ideological suspicions and idle fears, which were also reflected within the company. Any close connection with a foreign partner was met with great mistrust and concealed opposition, as is evident from the minutes of the meetings of the workers' council. At its session of July 9, 1968, the council had on the agenda the approval of the contract with Kautt & Bux. After the director read the contract and provided an extensive interpretation of individual provisions, all the hidden fears, distrust, objections, and reservations came to the surface. He was also assisted by the president of the municipality, whose presence at the meeting gave the agreement wider political support and the backing of the local political environment. It was the president who stressed several times that the contract was not the type of contract which allowed the exploitation of workers, and thus he rejected in advance the suspicions that could be felt from the tone of the speakers. The fear stemmed largely from the difference in the levels of wages in Germany and Slovenia and the reservations regarding the real prices of supplied raw materials and semi-finished goods. In modern terms, this meant that some of them saw in the envisioned partnership the danger of the effect of transfer pricing which Kautt & Bux could turn to its advantage in terms of its profit levels. The other reservations concerned

technology. Some members were quite impatient and objected to the gradual nature of the transfer of production. According to the plans at the time, they were first to produce commutators which required only minor adjustments to production and only later to switch to the production of more demanding types. After a lengthy discussion, they nevertheless reached a decision that Kolektor should sign the contract.

According to the contract, the Kolektor would invest all its available assets, and the foreign partner would invest cash, machinery, tools, the necessary know-how, experience, and goodwill. The investment ratio between the partners was at the upper limit what was allowed: Kautt & Bux could only obtain a 49 percent equity stake. Although the German partners wanted a majority stake, they had to accept this as the only possible option. But they insisted on a provision stating that, were Yugoslavia to adopt new legislation concerning foreign investment, Kolektor would agree to each of the two parties holding a 50 percent stake. The foreign partner also required additional assurances of the safety of its investment. They therefore negotiated the right to cosign any contract. Each contract had to be cosigned by a representative of Kautt & Bux's management. The term "codirector" was used in the contract. When responding to the ideological accusations regarding this delicate issue of a "codirector," Kolektor successfully explained to the authorities that the term itself was merely a "terminological concession." They explicitly assured that it would not have any consequences for the management of the company, as all other management structures typical of a socially self-managed company would remain in place. These explanations notwithstanding, this provision constituted a significant change in the structures and methods of company management and business.

Both partners were pragmatic enough that the cooperative undertaking proved very successful. In the period beginning with the conclusion of the contract and ending in the early 1980s, production and exports grew at an average annual rate of 12 percent. By the mid-1970s, the volume of production surged around eightfold, and around half of all commutators produced were sold to foreign markets through Kautt & Bux. The share of production for the foreign partner was slowly rising, and Kautt & Bux constantly exceeded the purchase value of commutators set out in the contract. Kolektor became a supplier to numerous European companies, including Philips, Bosch, AEG, Siemens, Vorwerk, and Perles. Moreover, thanks to the new technology, the door to the Yugoslav market was also opened wide. Kolektor had an 85 percent market share of the domestic market.

Kolektor increased its production, technology, and market share rapidly. It also constantly invested in research and development, and it enjoyed successes with a few patents which enabled it to lower production costs substantially. Kolektor also improved the educational qualifications of its employees. At the end of 1980, Kolektor has already surpassed Kautt & Bux by volume of production and overall operation, market share, and profitability. Kolektor went from being a recipient of knowledge to an innovator, a company which generated its own knowledge and started to base its further growth on this knowledge.

Then, in 1988, the first agreement, which had been signed 20 years earlier, came to an end. After initial disagreement, a new contract was finally signed which was very similar to the first agreement from 1968. But there was one important difference. Kolektor would be allowed to sell in markets where its German partner did not have its own company for the production or sale of commutators or its own sales agents. Thus, a small window opened for Kolektor for independent marketing with its own brand.

The 1990s were the challenging years for Kolektor and Kautt & Bux. The transition period in Slovenia and the business troubles faced by Kautt & Bux created a new context. During the post-1989 transition, it was finally possible to transform the Kautt & Bux share in Kolektor into a pure capital investment. Kautt & Bux achieved a majority share, 51 percent, with the lease of the production line to Kolektor. It was stipulated that Kautt & Bux's majority share should be reduced after Kolektor had paid off the production line. Kolektor did that in two years, so the share of Kautt & Bux decreased to 50.01 percent. Kautt & Bux at that time still held the exclusive sales and marketing rights for Kolektor's products on Western markets. Kautt & Bux regularly used its majority share in Kolektor as collateral in different credit transactions. In the new contract, there was a provision which later became crucial. Kautt & Bux agreed that for any kind of decision, a three-quarters majority of shareholders was required. This was a concession given to Kolektor in order to protect the interests of the Slovenian side.

In the beginning of 1990s, Kautt & Bux was overburdened with debts, lagging behind Kolektor technologically, and losing its competitiveness, and its market share was in decline. In fact, its business performance was completely dependent on the profitability of Kolektor. Kautt & Bux was at the verge of insolvency. Due to the marketing rights which Kautt & Bux held, which meant that it had direct contacts with customers, Kolektor had an interest in helping Kautt & Bux ease its solvency problems. However, in 1994, the efforts to keep

Kautt & Bux afloat proved futile. In fear for its future, Kolektor cancelled the agreement with Kautt & Bux, since Kautt & Bux was not in position to ensure the selling channels anymore. Within the customer's network, Kolektor was already recognized as reliable, innovative, and excellent producer of commutators. Although Kolektor faced initial troubles, it successfully managed to establish direct ties with its customers and build partnerships with them.

Simultaneously with the decline of Kautt & Bux, another process was going on, specifically, the privatization of Kolektor, or to be more precise, the privatization of Kolektor's 49.99 percent share, which was in state/social ownership. By the time of Kautt & Bux's bankruptcy, privatization based on the concept of broad employee co-ownership had started. After a very complicated procedure, two newly established companies (FI and FMR), owned by 800 employees with a deciding role in management, privatized the Slovenian part of Kolektor.

After Kautt & Bux declared bankruptcy, there was an offer to the Slovenian side to take over the Kautt & Bux share in Kolektor. At the time, however, the Slovenian side simply did not have enough funds for such a takeover. Finally, Kautt & Bux was taken over by Kirkwood Industries, an American commutator manufacturer, in February 1994. In addition to Kautt & Bux's total assets, Kirkwood also took over slightly more than a 50 percent share in Kolektor. Kirkwood entered the takeover procedure of Kautt & Bux, and Kolektor unprepared. Kirkwood's management expected to gain total control of the company. However, they were soon faced with reality. They found out about the contractual provision concerning the need for the assent of a three-quarters majority of shareholders for the adoption and enforcement of decisions. The bankruptcy administrator in Germany had obviously withheld this important information from Kirkwood.

In the 1990s, when Kirkwood acquired a share in Kolektor, Kolektor became even stronger and more independent. By using modern technology, it substantially increased its production capacity. The volume of production surged by 47 percent in the second half of the 1990s, from 66 million to 107 million commutators. In the same period, the volume of sales was up by 40 percent. The company started to establish commercial branches and production facilities in different countries (Germany, USA, Brazil, Mexico, South Korea, China, and Bosnia). In the end, Kolektor even bought Kautt & Bux.

From the perspective of the day-to-day realities, the story was not so smooth. The Kirkwood era at Kolektor was marked by huge misunderstandings

concerning the future of both companies, since they were also competitors on the most important markets. The Kautt & Bux and Kolektor management were on close and friendly terms. They trusted each other and were partners. In Kolektor's relations with Kirkwood, there was no sign of that spirit. From the outset, Kirkwood tried to subordinate Kolektor and degrade it into being a plain production plant, without any other function. This was completely unacceptable for the Slovenian side. Kirkwood attempted to acquire additional shares in Kolektor, but it failed, and it also underestimated the mutual loyalty in the local environment. After this failure, Kirkwood lost interest in Kolektor and in the European market. They offered Kolektor's owner the option to buy out Kirkwood's share. Slovenian owners agreed. They finished the procedure in 2002. At the same time, Kolektor also purchased the German company Kautt & Bux from Kirkwood and thus completely dominated the European market.<sup>21</sup>

### *Conclusion*

Yugoslavia was the first communist country to allow foreign investments in the form of joint ventures as early as the second half of the 1960s. The decision was made as part of the broad reform efforts of 1965. This was a period when the reformist wing of the LCY was dominant. The decision to allow foreign investments was part of the effort to modernize technology and management in the Yugoslav economy. The aim was to further Yugoslav integration into the global economy and the international division of labor and also to enable its competitive entry into the Western markets. Allegedly, the advantages for foreign enterprises of investing in Yugoslavia were the relatively lower investment costs due to cheaper labor and favorable tax rates, satisfactory infrastructure, proximity to the Western markets, a relatively extensive domestic market, and the possibility of exports to third markets, especially the Eastern Bloc countries. This was a pragmatic approach to making the domestic economy more efficient. However, the representatives of the reformist wing, even before they were removed from their positions at the beginning of the 1970s, had to take into account the political realities and the prevailing ideological orthodoxy. Therefore, the regulation of foreign investment was a compromise between pragmatism and the ideological constraints of the communist regime. For foreign investors, the security of their investments, shares and management of

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21 Lazarević, *Kolektor*.

joint ventures, and repatriation of profits were vital considerations. There were no ideological prejudices regarding the security of investments. This interest was recognized by the authorities, but there were greater concerns about the co-management of companies and the repatriation of profits. As of the mid-1970s, ideological restraints were tentatively weakening, and the regulation of foreign investments was gradually removing the constraints imposed by the self-management political and economic system. In the late 1980s, Yugoslavia fully liberalized foreign investment. However, at that time, the country's profound economic and political crisis drastically undermined the efforts to encourage foreign investments in the Yugoslav economy through liberalized regulation.

By 1980, Yugoslavia had managed to attract 200 joint ventures, which meant an average of around 15 foreign investments per year. These investments were rarely extensive, which attests to the caution of foreign investors when it came to joint ventures. 200 foreign investments were not much considering the size of the national economy, but they were a lot for a country with a communist system and regulatory restrictions. Research has shown that foreign investors had no problems with the Yugoslav self-managed corporate structure as long as the local or republic party leadership did not interfere. Investors received half of the management rights, even if they had a smaller share of the capital. Thus, both sides needed to seek consensus to make business decisions. A sort of an informal pattern emerged where the Yugoslav side had more say in setting the employee wages, determining the pricing policy on the domestic market, and focusing on integration into the local environment and relations with the local supplier network. Meanwhile, the foreign partner had a decisive say regarding the technology, the product range, the organization and quality of production, marketing, and sales on the Western markets. Together, they made decisions on recruitment, employee training, and marketing on the domestic market and in other communist countries. The experiences of foreign companies were mostly positive. The self-management of the Yugoslav companies was also not an obstacle. The qualities of the leading operational personnel of both partners were more crucial. The concerns of many investors regarding subordination to the workers' council as the supreme governing body of Yugoslav companies were unfounded. As a survey among foreign investors revealed, the workers' councils in joint ventures were more of an advisory body, while the decisions were made by the joint management board.<sup>22</sup>

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22 Artisien, *Joint Ventures in Yugoslav Industry*, 170–73, 188–93.

The volume of foreign investments shows that the expectations of the Communist Party's reform wing were justified and that foreign investment could be an important driving force for swifter economic development and the state's integration into the international economic space.<sup>23</sup> However, the restrictions put in place by the communist regime were severe. The ideological-political, social, and economic dilemmas related to foreign investments are evident from the case study presented here. The example of the Kolektor company shows that pragmatism was also needed by foreign investors and domestic companies in their daily business practices. The case of Kolektor also shows that foreign investment in a self-managed enterprise could be very successful when long-term objectives were given emphasis and there was minimal political interference, as was often the case in Slovenia.

As we have already pointed out, Kolektor was not a typical example, but the question remains as to how much of its long-term success was made possible by the investments made by its West German partner. The success of a company cannot simply be attributed to one or two factors. The answer lies in several arguments and their mutual interaction in a historical time and space. Each company is a specific, unique story. It takes place in a specific social context in combination with several favorable circumstances.

The presence of the foreign partner was no doubt a very important factor in Kolektor's success. It put Kolektor in a specific position and prevented any foreign interference. As for internal relations, here the foreign investor had an important controlling function. Dependence on the foreign markets guaranteed by Kautt & Bux and the ensuing steady incomes were advantages that could not be ignored. The need to adhere to the Western economic standards through Kautt & Bux also had a positive impact on the performance standard of the employees and the leading managers. The foreign partner assured a high level of investment. First, the high investment stemmed from the entry of the foreign partner and the requirements of the Yugoslav legislation, but later, they became a necessity guaranteeing technological progress and growth in the market share. Both sides were aware of this. The level of investments in development (knowledge), technology, and production were constantly high. Kolektor's success was founded on massive cost-competitive production in the constantly expanding electric motors market.

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23 Gnjatović, *Uloga inostranih sredstava*, 90–93.

Another important element was the stability of management and teamwork. In the period between 1968 and 1994, there were only two Slovenian directors and one German director. This contributed to the necessary predictability of the management and its approach to the business. Long-term goals had priority over short-term goals. This was respected by the foreign partner. Kolektor was a company which from the outset had a clear strategic orientation and clearly defined, realistic, and measurable goals. The loyalty of employees to the company should also be mentioned. The level of employees' identification with the company was high for a long time. The company tried to understand the employees and their families and help them meet their needs. This has been a constant feature of the company's policy of social responsibility, regardless of which decade of Kolektor's development we are looking at. Social responsibility was a key feature in the concept of Yugoslav enterprise, as other cases clearly show.<sup>24</sup>

Unlike most of the others joint ventures in Yugoslavia, the collaborative undertaking between Kolektor and Kautt & Bux was successful due to pragmatism of the partners, both the foreign and the domestic, and the pragmatism of local authorities, which was very important. Local party and administrative authorities respected the new reality at Kolektor, which was established after the entry of a foreign partner. Primarily, they were interested in economic performance, since Kolektor became an important employer and contributor to the development of the local community.

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24 Archer and Musić. "Approaching the socialist factory and is workforce," 44–66.

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