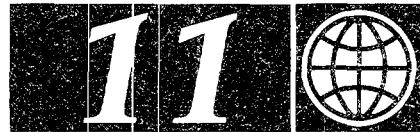


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World Bank Discussion Papers

Divestiture in Developing Countries

Elliot Berg
Mary M. Shirley

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The World Bank
Washington, D.C.

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SUMMARY

The objective of this report is to analyze the extent of divestiture in developing countries, review some of the obstacles and pitfalls, examine ways to overcome these problems, and consider the policy implications of the experience. It is not an exhaustive review; rather it is meant to be a first effort at expanding our understanding of divestiture in developing economies.

Divestiture can mean: (1) liquidation, both formal and an informal form of mothballing whereby operations are suspended, but the firm retains a legal and economic life; (2) privatization of ownership through the whole or partial sale of assets; and, (3) privatization of management through leases and management contracts. Privatization can also be a much broader concept, encompassing the general reassignment of property rights from the state to the individual, contracting out the delivery of public services to the private sector or cut backs in state activities to allow greater room for private initiatives, but these are beyond the scope of this report.

Governments divest for many reasons. One is a sense that the state sector is too big, that it is doing too many things that could be done more efficiently by the private sector, and that peripheral activities are diverting public resources, financial and human, from the priority activities of government. The hope is that divestiture will reduce the burdens on the state, while private ownership will lead to more innovative and efficient management of divested firms. Governments may also wish to sell shares in state enterprises as a way to increase popular participation in the ownership of national assets. Or, sales may be seen as a way to raise revenues. Finally, governments may wish to sell or liquidate money losers in order to reduce fiscal and credit pressures.

The review found few instances of formal liquidations in the 28 countries reviewed. (Most of the data are for the post-1980 period, with some exceptions: earlier instances in Chile, Bangladesh and Pakistan are included. See Tables 1-3.) Informal liquidations are much more frequent. Sales of large numbers of enterprises are also few, occurring in only two countries, Chile and Bangladesh. The review found that partial or total sales of assets in 15 other countries totalled fewer than 100 firms (all but eight of these were sales of all the enterprises' assets). Sales in most countries tend to affect those state enterprises that: (a) are small in terms of assets or employment, (b) were previously in private hands, and (c) operate in the manufacturing or service sectors. Few instances of leasing or management contracts were found, in part because the data are poor, in part because governments in developing countries have found such arrangements difficult to structure and manage successfully.

To some extent, the data underestimate the extent of divestiture. The review was principally a desk study; field investigations would probably turn up more cases. More importantly, divestiture is only now receiving attention in many developing countries, and this study may have missed more recent instances. Also, because of lack of data, the sale of shares held by public development finance corporations is not included.

The small numbers observed so far also reflect the obstacles and pitfalls to divestiture which are discussed in the text.

One obstacle to sales is the fact that governments in developing countries rarely want to sell profitable state enterprises, and the money losers they do want to sell are unattractive to buyers at prices or terms that government is ready to accept. Yet, if proceeds from sales can maintain social services and finance faster growth, or if private management could increase efficiency and tax revenues cost-benefit considerations could argue for the sale of profitable firms. The problem of negotiating a mutually acceptable price for money losers is related to another obstacle--the political opposition to the sale. While reform-minded decision makers and private individuals are often supportive, workers who fear for their jobs, officials who face loss of status and rents, others who expect that divestiture will favor the rich and privileged, will all be opposed. The controversy that surrounds the sale of state enterprises may make it politically risky for authorities to accept a large write down of assets.

Another obstacle is the few buyers that are acceptable to divesting governments, which may rule out purchases by foreign buyers or certain ethnic groups. Also, since capital markets are typically thin in developing countries, state enterprises must often be sold outright through private placement. If foreign sales are ruled out, it may be difficult for the domestic market to absorb the sale of state enterprises, which are often some of the country's largest enterprises. Another obstacle to sales and liquidation is an understandable unwillingness to lay off workers. But the resources used to fund these jobs could be used to create more productive employment elsewhere or fund social programs.

One of the pitfalls to be avoided is the risk of increasing the concentration of ownership where the range of buyers is small. Another is to extend special privileges to the buyer of a state enterprise. Subsidies or protection against competition keep the enterprise from operating in a fully commercial environment and protect nonviable firms from liquidation, thus defeating an important reason for divestiture.

A third danger is the risk that government will make a poor bargain. Managing divestiture can be tricky and the issues of whether and how to sell or liquidate are often ambiguous. A final pitfall may be to focus on privatization--rather than efficiency--as the ultimate goal. While there can still be efficiency gains from privatizing in a less than ideal policy environment or under monopoly conditions, the gains from changes in ownership will be much greater if the policy environment for private enterprises encourages competition, innovation, efficiency pricing, and the like.

The report documents ways governments are trying to overcome these obstacles and pitfalls. One is to develop strategies and action plans in order to anticipate and deal with problems. Clarifying objectives, costs and benefits can help to reduce political controversy by making sure the reasons for divestiture are well understood and the process is impartial and transparent. It has also proven helpful to set up appropriate institutions to take charge of the sale and to seek outside

expertise. In addition, some governments are simultaneously pursuing alternative, sometimes less controversial, forms of divestiture, such as leases.

The experience is limited but it provides some policy messages:

- (i) Divesting governments will need to take a strong position against giving special privileges to buyers of state enterprises that protect the firm from competition or make it perpetually dependent on government subsidies. The private buyer should assume the risk of operating in a commercial environment, including the risk of liquidation.
- (ii) The gains from privatization will be greater if the policy environment encourages efficiency in the private sector by promoting competition and efficiency pricing.
- (iii) Governments may need to create a special unit responsible for divestiture. Existing institutions may lack the administrative capacity or have a vested interest in keeping state firms public.
- (iv) Good technical advice from consultants, investment bankers and law firms--both foreign and local--can help governments in designing a strategy towards liquidation or sale, in valuing firms and negotiating with buyers, in structuring leases and management contracts.
- (v) Other forms of privatization--leases, management contracts, contracting out, deregulation--warrant further study to determine how they might contribute more to public sector restructuring programs.
- (vi) Transparency should be a part of all divestiture programs. This means more and better studies, more widely distributed in order to inform decision makers and the public of the reasons for divestiture. In many countries, the debate is too much about the costs of divesting--unemployment, increased imports, etc. Benefits need to be added to the dialogue if acceptance is to spread.
- (vii) Quiet, informal liquidation is an important form of divestiture in many developing countries. This slow "withering away" of nonviable enterprises should be encouraged, and eventually, formalized.

I. Introduction

1. State-owned enterprises (SOEs) have become important actors in developing economies. In a sample of 24 developing countries they are responsible for an average of 10% of gross domestic production and 30% of investment. They often dominate key sectors and internal and external trade; they are major borrowers in domestic and world credit markets; and they command a sizeable share of the budget. Consequently, more attention has been focused on SOE performance.

2. In many countries, developing and developed, this performance has not met expectations. Investments that were expected to spur growth and provide taxes and profits to the Government have become a drag on the economy and a drain on the Treasury. Governments, seeking value for the money they spend, are turning a critical eye on their SOEs, and in the process questioning whether the state enterprise sector is overextended, whether peripheral activities are diverting resources and attention from the core business of government, whether some SOEs have outlived or accomplished their objectives, and whether there are ways to tap private managerial and financial resources to accomplish public ends. Out of these concerns come a rising interest in the divestiture of state enterprises, as well as their rehabilitation and reform.

3. This review is concerned with divestiture of SOEs as a way to improve economic efficiency. Divestiture covers a range of activities:

- (a) Liquidation, which can be formal or informal. Formal liquidation involves the winding up of an enterprise as an entity and the sale of its assets. Many financially troubled SOEs are not liquidated in a formal sense but put into a form of mothballing; they suspend all or most operations but retain a legal and economic life.
- (b) Privatization of ownership through the whole or partial sale of assets. It is difficult to determine precisely at what point sales of equity lead to privatization of management. In Zambia, 50:50 joint ventures are invariably managed by the private partner, and in Portugal and Thailand, the management and performance of state firms with as little as 30 percent private shares differs considerably from wholly state-owned enterprises. The private shareholders are reported to have a stronger influence in the selection of the general manager than their minority position would suggest.

Note: This report is based on an extensive study by Elliot Berg with contributions from Helen Nankani, Boris Pleskovic, Charles Vuylsteke, and Marsha Wiss.

(c) Privatization of management through leases and management contracts.

4. Of course, privatization can be a much broader concept. The reassignment of property rights from the public to the private sector can take place without a sale and have important implications for management. For example, the most notable example of the transfer of certain property rights from the state to private individuals took place in Chinese agriculture. Contracting out the delivery of public services to the private sector, removing regulations that prevent private competition, shifting the financing of public services more to users, could also be defined as privatization. But these are beyond the scope of this review.

5. The objective of this paper is to document what is happening in the first three categories of divestiture in developing countries, and to examine the implications of this experience for governments and development agencies. This report presents the findings of an extensive desk study that relied principally on materials available in Washington, D.C., and limited case materials. It is meant to be a first step in expanding our understanding of divestiture in developing economies.

6. We first examine the reasons why governments divest in developing and developed countries, then analyse the record of divestiture in developing countries, review some of the obstacles and pitfalls and examine some ways to overcome these problems. Some policy implications of the experience are then considered.

II. Why Divest

7. The reasons why governments divest state enterprises differ among countries, and are almost always numerous. Some reasons are common to both developed and developing countries. The first is a sense that the state sector is too big, that it does too many things that could be done more efficiently by the private sector, that peripheral endeavors are diverting public money and managers away from priority activities of government.

8. The hope is that divestiture will reduce the managerial burden on the state while private ownership will lead to more innovative management which will see unfolding opportunity more quickly and seize it more aggressively. Such management will generally use resources more efficiently as well. While this entails some private, usually short run, costs, notably due to the elimination of redundant labor--the dynamic effects are expected to yield positive social benefits. Not only are nonviable private firms likely to have a lower survival rate than public ones, but the expectation is that common SOE management deficiencies will be reduced: slow decision making due to political-bureaucratic requirements, a preoccupation with processes rather than results, a neglect of markets and clients and a management environment in which reward is only

remotely related to performance. Moreover, financial transactions between government and private firms are expected to be more transparent, and hence more carefully considered, than with state owned companies.

9. Second, increased popular participation in the ownership of national assets is an important consideration in many countries. In industrial countries, privatization is seen as a way to bring stock ownership to the grass roots. For example, British Telecom's recent issue was accompanied by extensive advertising and special purchase schemes to promote a wide distribution of shares. Examples of privatization-to-promote-participation can also be found in developing countries. Chile's most recent effort to sell shares in SOEs to private investors is intended to increase participation, partly to raise the public's awareness of and pressure for state enterprise efficiency. Brazil is selling stock in its SOEs as a way to "democratize" ownership while raising capital.

10. Third, some governments see privatization as a way to raise government revenues. In the U.K. case, sales of shares in state enterprises since 1979 yielded over \$6 billion to the exchequer. Recent moves to sell equity in SOEs in Pakistan and Thailand, for example, have been justified in public discussion in part by the argument that the government may be able to raise substantial revenues.

11. For most developing countries, a major factor leading governments to consider a divestiture program is the desire to reduce fiscal and credit pressures. Authorities in these developing countries see divestiture as getting rid of unprofitable SOEs, those requiring budget subsidies and continued infusions of credit. For example, of the 61 enterprises that the Brazilian Government has proposed to sell to the private sector, most are unprofitable. Divestiture programs in Africa show even more strongly this tendency for divestiture to be viewed as a budget-relief and credit-reducing exercise.

12. Debt:equity swaps are also a potentially important form of divestiture which allow governments to simultaneously reduce the debt burden. Under these arrangements, investors typically purchase foreign debt at a discount and then exchange it for its face value in local currency which can be invested in, among other things, the purchase of equity in SOEs.

III. The Divestiture Record in Developing Countries

13. The data in Tables 1 through 3 (at the end of the paper) summarize preliminary information on the incidence of divestiture in developing countries. The data were obtained from a survey of published literature and World Bank reports and from interviews with staff of the Bank, IFC, IMF and AID. The meaning of each significant entry is explained in the footnotes to the tables. The data reflect the situation as of mid-1985; given the rapidly evolving policies in many countries there have undoubtedly been many recent changes.

14. This is one reason why the extent of divestiture is underestimated in these tables. There are other reasons as well. The numbers are not derived from field investigations in specific countries, except for Niger and Kenya. Because the published literature is so sparse, we could draw on it only for a few countries--notably, Bangladesh, Jamaica and Brazil. In most of these five cases of close study, more examples of divestiture are found than earlier observation had suggested. Moreover, interest in divestiture appears to be increasing rapidly in developing countries, judging from speeches and conferences on this topic. Many very recent sales or closures may have escaped attention. Also because some announced divestiture programs are aborted, we looked for reasonably hard evidence of action. In the process, reports of perhaps true divestitures have been rejected on grounds of insufficient or ambiguous evidence. Finally, because of lack of data, the tables omit the transfer to private ownership of shares in SOEs held by development finance corporations (DFCs), which may represent considerable privatization or reprivatization.

15. Despite all their limitations, the data in Tables 1-3 provide a more reliable, more comprehensive quantitative picture of what developing countries have so far done to divest SOEs than can be found anywhere else. And despite the long list of deficiencies and caveats which must make their interpretation tentative, some messages seem clear.

(a) Formal liquidations are very few. The review found hard evidence for only a handful--35 in about 30 countries. Formal liquidations occur most often in manufacturing, and seem particularly common in Africa.

(b) More common are informal liquidations. This category of liquidation covers a wide range. At one extreme are SOEs that are close to effective liquidation: few physical assets remain in workable condition; most staff has quit for other work; debt has been largely written off; small budget allocations, inventory sales, or part-time production finance a caretaker staff. At the other extreme are enterprises that remain physically intact and meet the payroll, but close most of their operations. Management may expect the enterprise to reopen, even though these firms may in fact be structurally nonviable. Of the total of 128 liquidations and closures recorded in Table 1, 70% seem to be of the informal type. Time will make many of them "real" liquidations. In Niger, for example, about half the 24 SOEs which Government intended to privatize in 1984 were in this condition. And in Togo, about 20, out of a total of 73 enterprises in the state sector, are closed. In Argentina, 12 of 29 SOEs up for sale in 1985 were closed down.

(c) Table 2, on privatization of ownership, confirms what has been observed by many: that so far substantial sales of assets and/or equity in SOEs have occurred only in a few countries. Excepting Bangladesh and Chile, the survey found fewer than 100 incidences of total or partial sales of all SOEs assets in 15 countries. (The table shows only eight instances of sale of part of an SOE's assets.)

(d) Sales have tended to affect SOEs that are small in terms of assets and employment. For example, in Brazil only one of the 17 firms or groups privatized as of 1985 had more than 1,000 employees. In Zaire 11 small farming units were sold to individuals; that, plus two

presumed sales of SOEs (not noted in the Table) make up Zaire's total sales. The 18 firms being considered for sale in Costa Rica employ less than half of 1% of the labor force. This is changing, however, as governments such as the Brazilian have begun to sell minority shareholdings in larger state firms such as PETROBRAS.

(e) Privatization appears to have occurred most frequently in manufacturing and service sectors. There has been little of it in utilities, mining or agriculture (excluding the considerable transfer of property rights in agriculture in China). Malaysia's planned divestiture of its telecommunications corporation is a first.

(f) Another striking fact about the record of divestitures is the predominance of "reprivatization" and the rarity of new privatizations. SOEs in developing countries typically fall into one of three main categories: formerly private firms that have been nationalized for essentially noneconomic reasons (nationalism or to create a socialistic system, for example); enterprises that have failed in the marketplace and been taken over by government; and SOEs that were created in the public sector and have always been there. Most of the sales in Tables 1 and 2 consist of enterprises in category one. For example, in Bangladesh almost all the divestitures were of enterprises "abandoned" by fleeing owners in 1965 and 1971. In Chile, the divested firms had virtually all been recently taken over (by the Allende regime). There are also some category two enterprises--firms that were formerly private, failed and were taken over by Government. In Brazil, 14 of the 17 privatized SOEs were of this type. (Also, DFC equity sales usually consist of firms of this type.)

(g) The number of incidents of divestiture by leasing, management contracts and joint ventures are surprisingly few. Management contracts are widely regarded as a minimal or first step in the privatization process--the privatization of management. Leasing is a highly flexible tool, which allows a disguised write-off of assets, by adjusting rental payments. It also permits retention of assets, so that crises resulting from temporary or cyclical factors need not cause sales at bargain basement prices. This was one reason the Seaga Government in Jamaica preferred to lease hotels in 1981 rather than sell them. Leasing of hotels is not unusual in developing countries (though rare in industrial countries), but in other sectors leasing is less frequent; the leasing of a steel mill in Togo and agricultural land in the Dominican Republic are interesting exceptions. This may be because leasing and management contracts can be hard to manage; costs are less transparent and the absence of an equity stake reduces management commitment to performance. The joint venture would seem to be an attractive instrument for a divesting government. Yet it is rarely used in this way. Private investors may prefer new joint ventures to participation in an existing, and often ailing, SOE. It may seem easier to prevent undue government interference in a new enterprise than to cure officials of their tendency to intervene in what was once a wholly public firm.

IV. Obstacles and Pitfalls

16. These patterns of divestiture raise some questions: Why are informal liquidations so much more common than definitive, legal liquidations and why are there so few actual sales in developing countries? One reason may be that divestiture is a new idea in most places and is only now becoming common. But clearly the small numbers observed so far also reflect the formidable obstacles that must be overcome and the pitfalls that must be avoided for divestiture programs to be implemented successfully.

17. Most of the obstacles to divestiture are familiar and need only be summarized here. Pitfalls are perhaps less well-known. They have only recently become clearer, as divestiture efforts yield some insights. But close, detailed assessments of post divestiture experiences are still rare even in countries where there is some experience to write about, such as Bangladesh and Chile.

18. Obstacles. The first obstacle is classic: rarely do governments in developing countries want to sell profitable SOEs and the money-losers they do want to sell can rarely find buyers at mutually acceptable prices. There is no inherent reason why governments should retain 100% ownership of money-making SOEs; if proceeds from sales of SOE shares can maintain social services and finance faster growth in troubled economies, then benefit-cost considerations could favor sales of equity in profitable enterprises. If private management can improve efficiency and profits further, then the state could benefit through taxation, the consumer through better (and possibly cheaper) goods and services, and the economy through the dynamism and expansion of the enterprise. This is apparently the view of some Malaysian officials, since they are divesting the profitable container operation in Port Klang, the port responsible for 80% of Malaysia's trade. They are also planning to divest two other major public enterprises, both profitable: the national shipping line and the national telecommunications enterprise, Jabatan Telekom, Malaysia's biggest SOE. Brazil is selling 5 billion shares in the profitable Petrobras oil monopoly to raise US\$400 million.

19. These examples notwithstanding, governments in most developing countries are mainly interested in selling unprofitable SOEs, which, with a few exceptions, are unattractive to buyers at prices or terms that government is ready to accept. Whether because of original error, poor subsequent management decisions or unfavorable technological and market changes, many of these firms are unlikely to be made financially profitable, even by better management. Thus, the plant may be too large for its potential market to ever work at full capacity or its technology may be too outmoded to permit it to compete.

20. This raises a second obstacle, one that has stalled divestiture programs in some countries: an inadequate awareness by political authorities that some enterprises they are willing to privatize are not economically viable, and should be liquidated. Some governments that have launched a divestiture program committed to sell ailing enterprises, draw back when it is discovered that many are not saleable on acceptable terms, if at all.

21. The second set of obstacles is political. Top decision makers and the local private sector may be favorable, but the opponents of divestiture are formidable:

- (a) The employed labor force is opposed. Overmanning is endemic in most SOEs and almost universal in troubled ones that are considered suitable for sale. One of the consequences of divestiture will be compression of the work force, and the affected workers know it.
- (b) Many officials are opposed because it reduces their area of authority, as well as the opportunities for patronage and corruption, and hence their status.
- (c) The intellectual community may be against it, and the ideological environment usually may be strongly unfavorable if the beneficiaries of privatization are perceived to be the rich and privileged.
- (d) Finally, political risks are high for the responsible authorities. These common political stumbling blocks are of three types. One is an understandable reluctance to lay off workers. The leadership may see that government resources used to perpetuate these jobs could be used to create more productive employment opportunities elsewhere or to fund social programs which benefit the poor. But these are longer-term possibilities, which must be weighed against the danger of social upheaval. A second political obstacle is the fear of being accused of stripping national assets. Where sales to foreigners are allowed, skeptics and political opponents will often shout "recolonisation." A third factor deepens these fears. Typically, there is a considerable difference between the original investment costs and the earning power of an SOE's assets, on which buyers' offering prices are based. The gap can be enormous; a Kenya molasses-gasohol facility that cost ShK 1 billion to build attracted no bid higher than ShK 5 million when it was put up for sale. All the factors which contributed to an SOE's low profits or losses--overstaffing, outmoded technology, outsized plant, poor location, etc.--cause buyers to deeply discount the enterprise's book value. Officials accepting a large write down of assets may face awkward questions about the original investment or accusations of corrupt dealing.

22. A third obstacle is the narrow field of potential buyers that are acceptable to divesting governments. In newly industrialized and middle income countries, foreigners are generally ruled out as purchasers. This is the case in the divestiture programs in Chile, Bangladesh, Brazil and Pakistan. In others, the share of ownership that foreign nationals can buy is limited by law or in practice. Even where no laws or explicit regulations prohibit it, many governments hesitate--even the most

outward-looking. Recently, the Ivory Coast Government pulled back at the last minute after agreeing to a land-leasing proposal because a non-national was involved.

23. In many countries, some resident groups are also regarded as illegitimate buyers of state enterprises, even if they are citizens. This is most evident in Southeast Asia, for Chinese minorities, and in East Africa, for "Asians" (mostly Indians). It is most explicitly a preoccupation in Malaysia, where national economic policy aims at favoring the Bumiputra--Malays and related groups.

24. Related to this is the fact that capital markets are typically thin. In the industrial countries, sales of stock have been the major instrument of privatization. Management buyouts and outright sale of companies are also common. These instruments find a much less promising environment in developing countries. Not only are capital markets thin even in larger countries and nonexistent in smaller, least developed ones, but also in many countries accounting, auditing and trading regulations are poorly developed, so the public distrusts the security markets. Hence, SOEs must often be sold outright through private placement. This makes it difficult for the domestic market to absorb the sale of SOEs, which are often some of the largest firms in the country. For example, the government that took office in Peru in 1980 announced its intention to sell some 60 SOEs in about three years. The market value of these enterprises was estimated at about US\$500 million, or about 3% of GDP. Peru's capital market could not absorb this amount of privatization in a short period of time without displacing other claimants for investment resources. And even if sales of this magnitude had been possible, the effect would have been to accentuate the concentration of wealth and income.

25. Pitfalls. There are also a number of pitfalls associated with privatization. First, divestiture may lead to greater concentration of ownership, especially when governments are hurried and the range of buyers is small. Chile, for example, sold between 133 and 400 SOEs (see notes to Table I) between 1974 and 1982. Most had been nationalized during the Allende period (1970-73). The post-Allende leadership wanted to divest quickly despite the deep economic recession prevailing after 1974. As a result, a few banking and industrial groups were able to pick up the bulk of the divested companies at low prices and for little equity. The total asset values involved were substantial--\$350 million in sales between 1974 and 1976, almost \$1 billion between 1974 and 1982. (The net worth of Chile's remaining SOEs was \$11 billion in 1982.) The sales increased the economic power of the 20 or so major industrial and banking groups; and closer control of industrial enterprises by banking groups led subsequently to severe distortions in lending policies.

26. A second pitfall is to extend special privileges to SOE purchasers (protection against external competition, tax holidays, subsidies, special access to funds or inputs, etc.) While some benefits may be justified (duty drawback privileges or a guaranteed right to repatriate profits), these should be carefully assessed. The private buyer should assume the risk of operating the enterprise in a commercial environment, including the risk of liquidation. Keeping alive firms that cannot survive without subsidies or special privileges, whether public or

private, only perpetuates the mistakes of the past. If the government is unwilling to let nonviable private enterprises die, then the sale of SOEs loses its meaning.

27. Third, there is the danger that government will make a poor bargain--a problem especially in the smaller, poorer countries. The divesting government is not in a strong position vis-a-vis potential buyers. It has made a public commitment to privatize, its enterprises are unattractive, it has little information or experience on the rules of this game (which are in all events poorly defined). There is a risk that low values will be put on SOE assets, and highly favorable financing made available to buyers. Special privileges attached to the privatized firm can create costly distortions and further drains on the Treasury as well as give noneconomic, possibly anti-development firms a new lease on life.

28. Managing divestiture is tricky and the issues of whether to sell or liquidate and how best to structure a deal are often ambiguous. For example, in March 1984 the Government of Togo leased a money-losing steel mill that had been shut down to a foreign entrepreneur. The arrangement gives the lessor rights to use the land, buildings and equipment for 10 years. The lease payments will cover less than 5% of the enterprise's annual debt service, and the overdue interest and penalties amount to more than the government will probably receive from the entire 10 years of operation. Meanwhile, the lessor receives a management fee and his corporation gets all profits after taxes. The pay-back period on his investment is about six months. He will also receive the audited book value of all improvements if the government doesn't renew the lease after ten years. The local cost of production exceeds the border price and the operation is financially profitable because of a 41% import duty. The lessor has other advantages: special privileges to import some competing products, duty-free import of raw materials, duty-free export of finished products.

29. On economic grounds, Togo might have been better off to close the mill and sell the equipment, even though costs of dismantling would have exceeded available selling prices, since government receipts from tariff revenues on imported steel would have exceeded its yield from the present arrangement. Moreover, prices to the construction industry are higher than they would be otherwise. On the positive side, over 150 Togolese have found employment and there are intangible effects whose consequences can't be predicted. The lessor, a dynamic entrepreneur, is busily seeking out new opportunities--in export of scrap for example. He may succeed in opening up new export markets. His presence has given Togo favorable publicity in the world press, which may attract other entrepreneurs whose talents Togo may be able to exploit more effectively.

30. A final pitfall may be to focus on privatization--rather than efficiency--as the ultimate goal. In the western industrial countries privatized firms are inserted into a private sector-dominated economy, and a well-structured policy setting with stable tax laws, an established and well-understood regulatory system, a large industrial (or service) sector with many firms and, in most instances, a reasonable degree of competition. In many developing countries the situation is different. The

policy and legal environments for private firms are often not accommodating; labor laws set down particularly constraining conditions. In many of the smaller developing economies, the SOEs are monopolies, and small market size rules out more than one firm.

31. For all these reasons, privatization in and of itself may not yield many efficiency gains. These will also depend upon the policy environment. For example, it may not matter much who owns an urban bus company if the state forces it to establish unprofitable routes and carry passengers at subsidized rates. What matters is the policy toward passenger operations. A dialogue about divestiture of a company under such conditions misses the point.

32. Similarly, private enterprise performance in many developing countries often depends heavily on government policy--on government allocations of foreign exchange (for input purchase and spares); on government-dispensed protection for its markets via tariffs and quotas; on government wage leadership for the wages it must pay; on government controls for the prices it can charge for its outputs. This is particularly so in economies where the private sector is small, in Sub-Saharan Africa, for example. The efficiency gains from changes in ownership under these conditions will be much greater if accompanied by other kinds of changes--altering exchange rate and monetary policies, deregulation, tariff and pricing reform, etc.

33. This does not mean that privatization can only affect efficiency in a perfect policy environment. For example, transferring a state monopoly to the private sector under the same government price control system could still improve efficiency. If prices remained the same, the new management would have an incentive to reduce the costs of the enterprise, adopting new technologies and more efficient production methods, since cost reductions would increase the profits of the new owners. Furthermore, the expectation of potential profits through rationalization of production and cost reductions would affect the price the private sector is willing to pay for an SOE. Thus the state could benefit from privatization even under conditions of continued monopoly. But the gains will be greatest when the policy environment encourages competition, innovation, efficiency pricing, and the like.

V. Overcoming Obstacles and Avoiding Pitfalls

34. A critical question is how to design privatization programs that will maximize potential benefits and avoid errors. Some efforts to overcome problems associated with divestiture include:

- (i) preparing the ground for divestiture,
- (ii) developing systematic divestiture strategies and classifying SOEs,
- (iii) "readying" SOEs for sale or liquidation,
- (iv) creating special units responsible for divestiture,

(v) using outside assistance, and

(vi) privatizing by means other than the sale of assets

Clearly, this list is not complete; there are many other aspects of this process that are not discussed. Unfortunately, not much has been written on the process by which developing countries have sold SOEs--the strategies followed, the institutions involved, the procedures for locating buyers and arriving at a deal, etc.

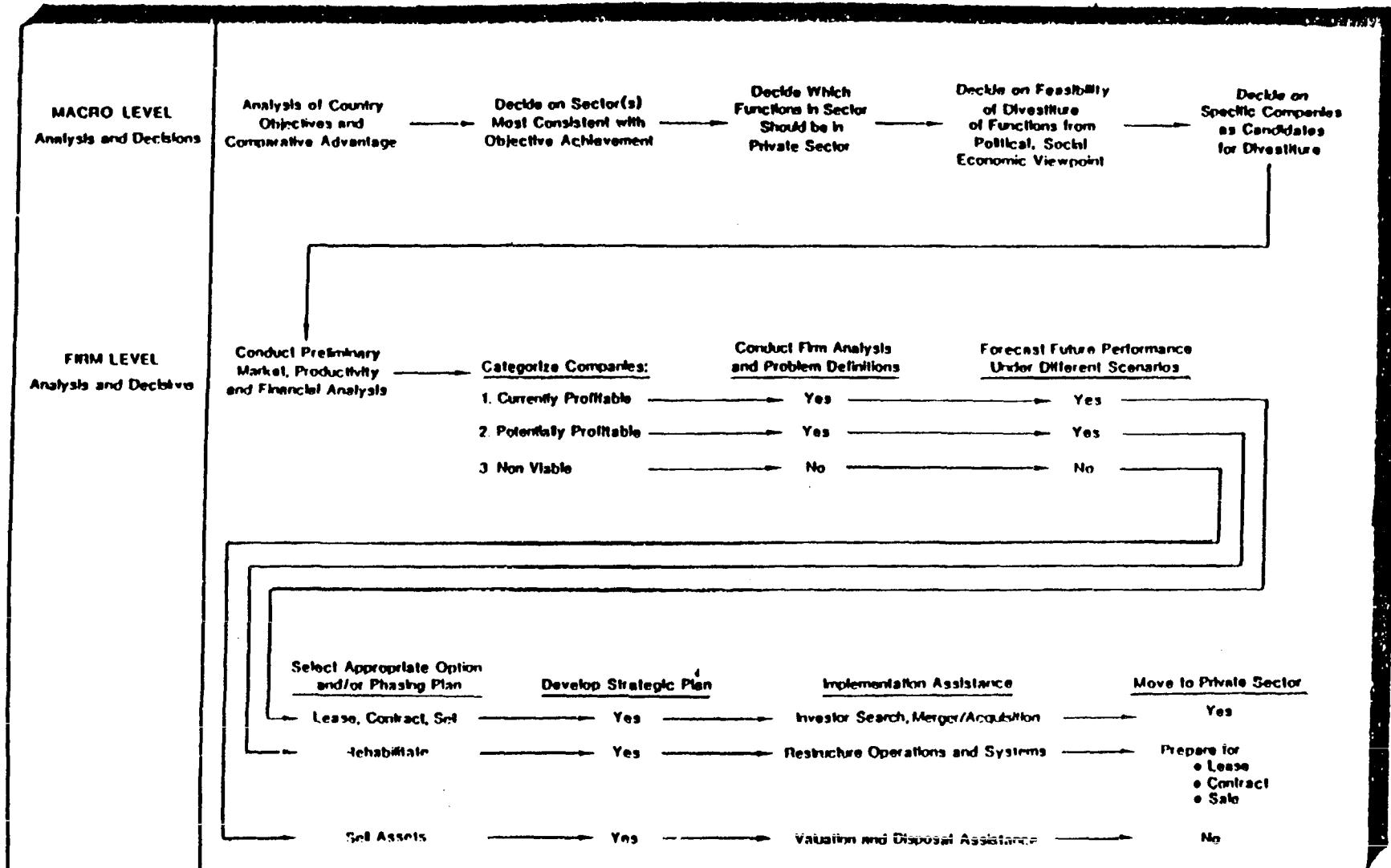
35. Preparing the way. One of the ways to avoid obstacles and pitfalls to divestiture is for government to clarify its policy first, to make explicit its objectives and priorities. The political opposition to divestiture may be reduced if the reasons are well understood and the process, transparent and impartial. In Peru, for example, the Government conducted a series of studies and a public education campaign to prior to liquidating part of its fishery SOE. A commission composed of representatives of the Ministry of Fisheries, the Central Bank, the Industrial Bank, the Ministry of Economy and Finance, and the private fisheries sector first studied the problems and made a series of recommendations. Arrangements were then made to pay bonuses to workers who voluntarily resigned. The workers were informed of their rights under the new arrangement and newspapers were provided with information documenting the disappearance of the raw material from Peruvian waters and the cost to the State of operating a fishing fleet and fish processing plants at less than one-third capacity. As a result, despite protests by some union leaders and politicians, 4,800 workers out of 6,000 resigned and 29 out of 36 plants were shut down, all with widespread public support.

36. Systematic strategies and classifications. Another approach is to try to anticipate problems and pitfalls by designing a comprehensive and systematic strategy and classifying SOEs according to carefully thought-out criteria, taking account of the economic and social environment. Chart 1 presents an example of a scheme for organizing a divestiture program. This scheme (developed by Cooper and Lybrands) moves from the macroeconomic environment (country objectives, classification of enterprises, decision on candidates for divestiture, etc.) to the enterprise level. Each firm that might be divested is analyzed and classified again according to profitability. An action plan is then developed for each. Some firms can be divested right away; a search for investors is the specified action. Some will be rehabilitated for future sale. Nonviable enterprises will be liquidated; for these, assets have to valued and arrangements made for sale.

37. An alternative approach developed by the World Bank to assist the Government of Turkey gives more emphasis to the sector policy changes (pricing, tariff reduction, elimination of barriers to entry, subsidized credit, etc.) needed for effective privatization. It also emphasizes the need to proceed with specific industrial studies and preparation for action even while the overall plan is being developed. The main steps can be summarized as follows:

- (i) Establishment of objectives, policies, priorities and guidelines for the privatization program.

Chart 1
Critical Decision Path To Divestiture Options



Developed by Coopers & Lybrand

- (ii) Proposals to solve major legal, administrative, fiscal, organization, policy and other obstacles standing in the way of privatization.
- (iii) Classification of SOEs into different groups according to their prospects for privatization.
- (iv) Establishment of a broad privatization action plan with SOEs ranked in order of priority. The action plan would define which enterprises or individual plants and assets: (a) could be sold immediately; (b) would need rehabilitation before sale; (c) should be considered for leasing and management contracts; (d) should be considered for closure; (e) should remain as a SOE, etc. Furthermore, the plan would spell out a timetable and the major policy decisions to be taken by the Government to initiate the implementation phase for each SOE.

38. In Jamaica an approach proposed by the Jamaica National Investment Bank (done with the assistance of Management Analysis Center, a management consulting firm) classifies SOEs into three groups: Type A companies, which are clear candidates for divestiture within three to five years; Type B companies, which are "strategic," and will not be divested; Type C companies about which there is no clear consensus. The following criteria are proposed for choice of initial divestiture targets:

- large asset base (to ensure high purchase price);
- viable product(s) and market(s) (to ensure attractiveness to potential buyers);
- large financial losses (to maximize economic benefit to government from divestiture);
- minimum need for short-term employment reduction (to ensure minimum negative social effects);
- minimum government-owned or government-guaranteed debt (to facilitate terms of sale);
- minimum need for majority foreign ownership (to minimize possible political opposition).

39. Evidence on the effectiveness of these systematic approaches is not yet in; most of these designs still remain in planning stages. In the Jamaica case, the program has moved forward very slowly. The extensive divestiture efforts in Bangladesh and Chile did not begin with these kinds of classification schemes, in part because they involved much reprivatization. The more comprehensive the approach the slower the process is likely to be, and the more costly. But the better information base can improve the quality of decisions, and the fact that divestiture is part of an overall SOE reform can make it more palatable politically.

40. On the other hand, much can be said for a quicker, more enterprise-focused approach. In most cases, the government is considering divestiture primarily to reduce SOE absorption of budgetary and credit resources. But few of the major money-losers and credit-absorbers are ever included on anybody's "to privatize or liquidate" list--the railways, for example, and the utilities. The smaller firms in the industrial sector, most of which have probably seen budget subsidies and bank credit shrink and are withering away, are also not prime candidates. The top candidates are usually predictable--sugar, cement, fertilizers, petroleum refining, for example--and smaller import substituting industries that produce little domestic value-added. Thus the potentially marketable SOEs can be identified relatively quickly, without lengthy formal classifications. Furthermore, the decision on whether to sell or to liquidate is seldom faced squarely in any divestiture program. Officials will usually insist that enterprises to be divested should all be sold. Analyses showing that these either cannot be sold (at acceptable prices), or should not be sold because they are not economically viable, are rarely put forward and the "To Liquidate" column in the classification table is only sparsely populated. Moreover, these formal schemes may interfere with informal closures if authorities feel encouraged to take SOEs out of mothballs in a possibly vain attempt to sell them. In the end, the choice of approach must be made on a case by case basis, be suited to the political atmosphere and tailored to country circumstances.

41. Readyng SOEs for Divestiture. Once a list of candidates for divestiture is agreed on, the target entities will have to be "readied" for sale or liquidation. Careful attention to this process can avoid future headaches. Some of those to be privatized are usually not in appropriate legal form. Statutory bodies or government departments have to be legally transformed into joint stock companies.

42. The process should also include the buildup of a full dossier on the enterprises to be sold or liquidated for presentation to potential buyers. Assets will have to be valued and net claims on those assets determined. This may require additional financial audits; in some enterprises, especially those that have been informally closed for some time, there will frequently be no recent balance sheets or profit and loss statements. The claims of employees will have to be determined; even those no longer working in "closed" enterprises may retain legal rights to jobs and/or severance pay. Unrecorded arrears have to be uncovered to prevent unwelcome future surprises. There may be unknown liens outstanding and many unresolved legal issues, most of them unfamiliar in industrial country divestiture experience. In Togo, for example, some expatriate shareholders in divestable SOEs have departed to points unknown: What liabilities does the divested enterprise have with respect to these people? The Malaysian rule limiting foreign equity ownership to 30% of the total was a roadblock in that country's plans until amended.

43. Often a key question at this juncture is whether to invest in rehabilitating the enterprise's plant prior to sale. Potential SOE buyers questioned in Peru and Mali, for example, preferred a lower price to buying a rehabilitated plant. They feared that government would not make wise investments and would have unrealistic expectations about the sales price.

44. An important form of preparation in Britain was the installation of a first rate chief executive who would be accepted as an ideal choice for the newly privatized company. The executive helps create an internal momentum for divestiture to overcome the opposition from organized labor and others. This has been rare in developing countries, where salary rigidities and the poor conditions of many SOEs make it hard to attract such talent. Under such circumstances, it becomes especially important to put talented, dynamic people in the unit in charge of the divestiture program (see below).

45. Divestiture Units. Experience suggests the desirability of a central administrative unit to manage the divestiture program. In Bangladesh, the scene of probably the most successful divestiture experience, a number of special organizations were created: a "Scrutiny Committee" to verify titles and nationalities of former owners; a Working Group on Disinvestment to value assets and recommend selling prices to a "Divestment Board", which made final decisions. A similar kind of structure was set up in Jamaica in the early 1980s, when a divestiture effort was initiated there. A Joint National Investment Commission (JNIC) was created, assisted by a Divestment Secretariat. All divestiture proposals are to be reviewed by the JNIC. In addition, a high-level Divestment Committee, named by the Prime Minister, vets all proposals. This Committee consists of four public officials and four representatives of the private sector. Its function is to increase transparency of divestiture operations. Togo has created a "Committee to Evaluate Privatization Offers" which advises the Ministry of State Enterprises after scrutinizing offers on eleven enterprises up for sale. The Committee is composed mainly of civil servants, with representation from political leaders, the Chamber of Commerce and the private banking sector.

46. Although there is the risk of creating a large bureaucracy (though in fact only a small group is necessary), these units have several advantages. One is to vest responsibility for privatization in a group with an interest in its success. Typically, ministers have little incentive to reduce their power base by eliminating their SOEs--quite the contrary. Another virtue is to have a body able to do the analytical work to decide whether liquidation is socially preferable to sale and to encourage economically rational choices about such critical issues as the terms of the sale, subsequent privileges for buyers (tariffs, access to imports, etc.) and the participation of non-nationals.

47. The bargaining position of governments engaged in negotiating sales could be strengthened if the divestiture unit has in hand analyses of the costs and benefits of the various elements in the package: the earning power of the firm's assets under various assumptions about input costs and product mix (assuming improved management) and the private and social costs and benefits of retaining or increasing each of the privileges that comes with the firm. Finally this unit can help engender intellectual and political acceptance of the program. For example, it can calculate the price of keeping nonviable enterprises open to provide unproductive employment for what is usually a small and relatively well paid part of the labor force. The net benefits of sales, even sales below costs, in terms of more dynamic management, removal of bottlenecks, stopping a drain on the Treasury, increasing competition and efficiency, can be explained.

48. Foreign Assistance. Donors have begun to help finance advisors, both foreign and domestic, to divesting governments. Outside expertise can play an important role in advising governments on alternative ways to divest SOEs, valuing assets, identifying potential buyers, structuring and negotiating deals, and generally acting as "honest brokers." Investment banks, consulting and law firms, both domestic and foreign, and the IFC can provide this expertise; the fee for such services is typically higher than for other forms of consulting. Outside experts can not only assist government to strike a good bargain, but can sometimes help to reassure government and the public about the impartiality and integrity of the process. Private investment banks are eager to advise on sales, but have been less willing to purchase shares. IFC is also able to advise and is contemplating taking equity in some cases.

49. One of the obstacles to sales signalled earlier is the opposition of the labor force. Another is the fact that many SOEs carry heavy indebtedness to suppliers and to government. USAID is implementing an aid program for Costa Rica to try to address these problems. The counterpart funds generated by an Economic Support Fund grant of \$140 million are being used to set up a private trust to buy 18 public enterprises owned by the Costa Rica Development Corporation (CODESA) on the basis of prices negotiated with the Controller General. The trust will then sell shares of these companies by public bidding. Prior to sale, CODESA will assume the outstanding debt of the companies using credit from the Central Bank. This should smooth the divestiture process by reducing the potential for legal claims against operating company assets. Some of the proceeds from the sale will be used to compensate employees put out of jobs by the divestiture. Proceeds will also go to the Central Bank to reduce CODESA's indebtedness.

50. While such donor schemes can remove some obstacles to divestiture by relieving the burden of arrears and some severance obligations, they obviously carry potential political risks. Foreign assistance in such a delicate area might be regarded as encroachment on sovereignty, and add to the usual opposition to divestiture. There is also concern that the sale of shares to large economic groups would increase oligopolistic power in the small Costa Rican economy.

51. Other Forms of Privatization. Privatization other than by the sale of assets is less controversial, can be done gradually, need not strain the domestic capital market, increases competition and avoids the embarrassing write down of assets. Not only management contracts and leasing, but also contracting out of services, cutbacks in SOE activities, and deregulation in general all increase the private management of previously public activities. While the latter were beyond the scope of this review, a few examples can illustrate how these approaches can increase the role of the private sector.

52. Public bus monopolies can often be replaced by competing public and private, or purely private, bus companies. For example, in Kingston, Jamaica, bus services were provided by a private company, the Jamaica Omnibus Service (JOS), between the early 1950s and 1974. The JOS was a profitable operation over most of this period. However, mainly because it was obliged to operate longer routes and extend service to areas with

little traffic, profitability declined and services deteriorated. In 1974, the company was taken over by government. Under government management productivity fell, costs increased, and services went from bad to worse. Unreliability of JOS scheduling was frequently blamed for extremely high rates of lateness and absenteeism experienced by workers in Kingston. Deficits soared: by 1983 deficit financing amounted to more than US \$1 million a month; by 1982, accumulated operating losses exceeded total equity value. Dissatisfaction with poor service was so general that government in effect deregulated the industry; it allowed a parallel, minibus-based transport network to develop, and, in fact, licensed minibus operators. Government cut back JOS responsibilities. It proceeded to lease most of the assets of the JOS to private operators and auctioned off the company's primary routes to private operators. The JOS still exists as a legal entity and it retains some regulatory functions, but it is no longer operating buses.

53. Turkey proves another good example of the effects of cutbacks in an SOEs activities and support, combined with deregulation and promotion of the private sector. The Meat and Fish Organization, (EBK), is one of that country's largest public enterprises. It is a meat processing corporation that until 1980 enjoyed a virtual monopoly on imports and exports of meat, and was the only source of modern meat processing facilities. Despite its privileged position EBK was a recognized failure. In 1983, it provided only 11% of the total national supply of processed meat, and was deep in debt to suppliers of live animals. Many of its important customers--the armed forces for example--were late payers. Its slaughterhouses worked at less than 25% of capacity, well below break-even points. Its losses mounted and by 1983 it had the highest total indebtedness of all Turkey's SOEs, and negative net worth.

54. Starting in 1980 government policies transformed the situation in meat processing. EBK lost access to the subsidies that it once received through various special funds and accounts. Instead it had to seek credit from the Central Bank, which--in line with the new general guidelines--lent at market rates of interest, presently about 50%. The EBK was effectively precluded from access to credit by this means. A second change was the legalization of private sector meat processing operations. In addition, special export promotion incentives were given to the private sector. By 1984, 31 new companies had applied for licenses to construct processing facilities and 18 existing companies had sought approval of their present facilities.

55. As a result of these changes, EBK is unraveling. Since 1980, a number of its slaughterhouses have been closed. Thus a particularly deep-rooted and well-entrenched public monopoly, which for decades has generated rents and absorbed large volumes of public sector resources for unproductive uses, is in the process of withering away. It is a striking example of change wrought by budgetary/credit constraints and deregulation.

VI. Implications for Policy

56. The experience is limited but it provides some policy messages. First, divesting governments will need to take a strong position against special privileges for purchasers of SOEs. National authorities should not agree to make bad investments profitable by retaining, or even adding to, any special benefits and privileges that may have been attached to the enterprise when it was in the public sector--protection from competition, tax exemptions, special investment credits, sheltered domestic markets. Otherwise, these enterprises will present recurring future demands for special favors; they will be perpetual claimants for public money and the attention of the national authorities.

57. Second, the gains from privatization will be greater if the policy environment encourages efficient operations of private enterprises. Reforms to promote competition and efficiency pricing (antitrust legislation, reductions in protection against imports, elimination of privileged access to credit and inputs, pricing deregulation and the like) should be part of the effort to encourage efficiency.

58. Third, divestiture requires a special administrative capacity seldom found in existing institutions. Moreover, many SOE oversight agencies have a vested interest in keeping the enterprises in the public sector (and thus adding to their prestige and power). The creation of special units to manage the process has worked well in divesting countries in the past.

59. Fourth, better technical advice could help divesting governments. For example, investment bankers have played a key role in many developed country sales of SOEs and are beginning to be active in some developing countries (Turkey, for example). Additionally, the lease arrangement, which has the great advantage of leaving asset ownership unchanged while permitting a write-off of asset values, could be made more serviceable and less risky to governments if good technical advice were at their disposal. For management contracts, there are well defined rules of the game, for a few industries at least. Thus a government negotiating a hotel contract can go to a "Red Book" for standard provisions; it is much the same with petroleum. And in both these industries there are specialized consultants who can be called upon to advise governments. But for leases there is very little guidance available, even for hotels. A donor technical presence could improve terms obtained by leasing governments, and a donor financial presence could help insulate leasing decisions from undue political interference.

60. Fifth, privatization of ownership has been the principal element of the divestiture programs studied here. Yet there may also be considerable scope for other forms of privatization, that leave intact public ownership. The reasons why these options have not been used much need to be better understood and ways found to make them operational. In addition to leases and management contracts, privatization in its other dimensions may be able to contribute more to public sector restructuring programs. Deregulation, contracting out of government services, private provision of "public" services--education, health, water supply, agricultural expansion, agricultural inputs generally--all warrant further study.

61. Sixth, transparency should be a major element in all divestiture-related programs. This means more and better studies of individual problem enterprises, and wider distribution of their findings. It can happen, and probably happens fairly frequently, that technocrats recommend liquidation of an enterprise without a study in hand that will persuade skeptical and hesitant decision-makers that the enterprise truly is beyond salvation, or at least that the costs of attempted rehabilitation are likely to be prohibitive. Moreover, the divestiture process involves a broad writing down of national assets. It necessarily entails public admission that investment resources were wasted. Detailed and technically unimpeachable information, widely distributed, can play a larger role than is now common in divestiture strategies. More should be known about how much explicit and implicit subsidizing goes on, and the costs in foregone activities. It should be clarified that some transition costs may have to be met regardless of ownership; if the firm is to be efficient, excess labor, for example, may have to be laid off whether the firm is public or private. The liquidation debate in most countries is too much about costs--unemployment, increased imports, and abandoning islands of modern technology. Benefits have to be added to the dialogue if acceptance is to spread.

62. Finally, and notwithstanding this stress on transparency and sound technical studies, experience has shown the importance of quiet, informal divestiture as an interim step. Public scrutiny and study of these arrangements may be their undoing. True liquidation of a nonviable SOE--in the sense of shutting it down, laying off the workforce and selling its assets--is preferable to mothballing since it frees more resources and assures that the enterprise cannot easily rise from the ashes. But, as the data show, this final solution is hard for governments to accept. Second or third best solutions are unavoidable in such a highly politicized area. Care should be taken not to replace informal actions with formal commitments, but rather to monitor informal closures (especially, the shrinkage of the wage bill), study the viability of the firm and eventually move to final action.

63. This paper is a first effort to understand the extent of divestiture in developing countries. As such, it has raised as many issues as it has addressed. The divestiture experience in developing countries needs to be analyzed in more detail in order to: review the different approaches followed and the results; determine how policy questions were treated and the effects; understand the impact of divestiture on the performance of the firm, on the sector, on investment and income; and glean any wider lessons for other developing countries. Better guidance is needed not only on the technical aspects of sales, but also on the economic issues of divestiture: what are the costs and benefits; how should priorities be set to maximize efficiency gains; will a sale divert resources and entrepreneurial skills from new investments with higher returns; how can safeguards be built against some of the risks, such as strengthening oligopolies, or exploitation and abandonment of a necessary service. Other forms of privatization--leasing, contracts--need to be studied further to determine why these options are infrequently chosen and whether and how they can be made viable alternatives. Ways should be sought to increase the returns to resources, public or private, by changing the policy environment and enhancing the incentives for efficiency by

encouraging competition. Finally, since many SOEs are likely to remain public, particularly natural monopolies, ways to improve their efficiency should also be studied.

64. Systematic efforts by developing countries to divest state-owned enterprises are very new, and available experience still too little understood to allow strong conclusions as to their effectiveness or future potential. Nevertheless, it is apparent from the accumulating body of experience that divestiture has so far been a little-used instrument. Yet the rationalization of the state sector can be a potential source for renewed growth in many countries. With the lower growth rates typical of the 1980s, the slow increase or stagnation in budget resources, constrained credit due to economic stabilization needs, and less resources available for new investment, it is now imperative to make the most efficient use of existing resources. Divestiture can bring about more efficient and dynamic management and can free public resources, both financial and managerial, for more efficient uses.

TABLE 1: LIQUIDATIONS AND CLOSURES OF STATE-OWNED ENTERPRISES,
BY COUNTRY AND SECTOR (1)

| REGION/Country | Dimensions of SOE Sector | | | Liquidations & Closures | | | Sector | | |
|----------------|--------------------------|---------------------|----------------------------|---------------------------|--------------------------------|-----------------------|-----------|-----------|----------|
| | Total Number | Value (% of GDP) | Invest. Added (GFCF) | Number (% of Employed) | Number of Liquid- ations | Number of Closures | Manufact. | Agricult. | Services |
| | | | | (000) | | | | | |
| AFRICA | | | | | | | | | |
| Cameroon | 80 | | | | | 5 c) | 5 | | |
| Ghana | 130 | | 57 | 40 | | | | | |
| Guinea | 65 a) | | | 130 | | 16 b) | 16 | | |
| Ivory Coast | 113 a) | | | 186 | | 10 c) | | 3 | 7 |
| Kenya | 180 | 8 a) | | 17 | | 5 | 3 | | 2 |
| Liberia | 23 | 8.5 | 20 | 12 | | | | | |
| Madagascar | 130 | | | | | 5 | | | |
| Mali | 54 | | | 14 | | 9 a) | 4 | 2 | 3 |
| Mauritania | 108 | 20-25 | | 130 a) | | 4 b) | 3 | | 1 |
| Niger | 54 | 10 | 87 | 13 | | 3 | | 1 | 1 |
| Senegal | 104 | 20 | 40 | 134 a) | | 25 | 24 | | 1 |
| Sierra Leone | 26 | | 15 | 13 | | 1 a) | | | 1 |
| Somalia | | | | | 3 | | | | |
| Sudan | 136 | 40 | NA | 1600 b) | | 10 | 8 | 1 | 1 |
| Togo | 73 | | | (5-7 a) | | 9 | 9 | | |
| Uganda | 130 | | | | | | | | |
| Zaire | 138 | | | 148 | | 3 | | | |
| LAC | | | | | | | | | |
| Argentina | 29 | | | | | 12 | | | |
| Brazil | 547 | | | 11,500 | | 9 | | | |
| Chile | 421 | | | | | | | | |
| Mexico | 378 a) | | | | 10 b) | | | | |
| Panama | 45 | | | | | 2 | | | |
| Peru | 142 | | | | | | | | |
| OTHER | | | | | | | | | |
| Bangladesh | 778 a) | | | | | | | | |
| Pakistan | 75 a) | | | | | | | | |
| Sri Lanka | 43 | | | 166 | | | | | |
| Turkey | 65 | | | | | | | | |
| Thailand | 70 | 10 | 37 | | 2 | | | | |

(1) Wholly-owned SOEs unless otherwise noted. Data refer to post 1980 period except as noted in footnotes following tables.

TABLE 2: SALES OF STATE-OWNED ENTERPRISES, BY COUNTRY
AND SECTOR (1) (NUMBER OF SOEs)

| REGION/Country | Targeted Sales (2) | Actual Sales (3) | Sector | | | |
|----------------|--------------------|------------------|--------|------------------------------------|---------------|-------------|
| | | | Total | Of Which Partial Sale of Equity | Manufacturing | Agriculture |
| AFRICA | | | | | | |
| Cameroon | 12 b) | | | | | |
| Guinea | 43 c) | | | | | |
| Ivory Coast | 20 c) | 4 d) | | | 2 | 2 |
| Liberia | 7 a) | | | | | |
| Madagascar | 15 | | | | | |
| Mali | 11 b) | 2 c) | | | 1 | |
| Mauritania | 10 c) | 1 d) | | 1 | | |
| Niger | 24 a) | | | | | |
| Senegal | 10 b) | 5 c) | | | 3 d) | |
| Sierra Leone | 10 b) | | | | | 2 |
| Sudan | NA | 7 | | | 7 | |
| Togo | 40 c) | | | | | |
| Uganda | 67 a) | | | | | |
| Zaire | 37 b) | 11 | | | | 11 |
| LAC | | | | | | |
| Argentina | 27 | | | | | |
| Brazil | 155 | 17 | | | 9 a) | |
| Chile | | 133 | | | | 8 |
| Jamaica | 30 | 2 | | 1 | | 2 |
| Mexico | | 8 c) | | | | |
| Panama | 5 a) | 1 b) | | 1 | | 1 |
| Peru | 60 a) | 3 b) | | 3 | | |
| OTHER | | | | | | |
| Bangladesh | | (217 b) | | | 70 | |
| Malaysia | | 4 a) | | 2 | | 4 |
| Pakistan | | 6 b) | | | 6 | |
| Sri Lanka | | 11 a) | | | 2 | |
| Thailand | | 3 b) | | | 3 | |

(1) See footnote to Table 1.

(2) It is difficult to define "targeted" or "potential" sales precisely. In this table, one of the following three definitions has been used:

- i) target set by the government in question, as reflected in an official statement;
- ii) recommendations and/or suggestions made by World Bank staff in reports focussed on SOEs;
- iii) a combination of Government statements and agreements with the Bank under Structural Adjustment Loan or Credit Conditions or some other agreement.

(3) Excludes sales or transfers of shares in SOE held by state development finance corporations.

Footnotes follow tables.

TABLE 3: OTHER DIVESTITURE EXPERIENCE: LEASING, MANAGEMENT CONTRACTS AND JOINT VENTURES (1)

| REGION/Country | Leases | | | Management Contracts | | | Joint Ventures | | | |
|---------------------|----------|--------|------|----------------------|----------|-----|----------------|--------|------|---------|
| | (Number) | Sector | | (Number) | Sector | | (Number) | Sector | | |
| | | Man. | Agr. | | Service | | | Man. | Agr. | Service |
| AFRICA | | | | | | | | | | |
| (Cameroon | | | | | (6-10 c) | 5-9 | | 1 | | |
| (Guinea | 1 d) | | | 1 | | | | 3 | 38 | |
| (Ivory Coast | | | | | (3 e) | 3 | | | | |
| (Liberia | | | | | 1 | | | | | |
| (Madagascar | 5 | | | 5 | | | | 2 | | 2 |
| (Mali | | | | | 1 | | | (2 b) | | |
| (Sierra Leone | 4 c) | | | 4 | | | | | | |
| (Togo | 3 d) | 3 | | | (4 e) | | 4 | | | |
| (Zaire | | | | | (3 c) | | 3 | | | |
| LAC | | | | | | | | | | |
| (Dominican Republic | 1 a) | | 1 | | | | | | | |
| (Grenada | 1 a) | | | 1 | (1 b) | | | 1 | | |
| (Jamaica | 2 | | | 2 | 12 | 3 | | 9 | | |
| OTHER | | | | | | | | | | |
| (Bangladesh | | | | | 1 | | | | | |
| (Pakistan | | | | | | | | 2 | 2 | |
| (Sri Lanka | | | | | 5 b) | 5 | | | | |
| (Thailand | 1 c) | 1 | | | | | | (2 d) | 1 | 1 |

(1) This Table is incomplete, especially with respect to management contracts, of which there are undoubtedly many that escape attention because of their undramatic character. The incidence of leasing arrangements is similarly understated, though these have been somewhat less difficult to trace. See footnote to Table 1.

* Note: This refers to mining.

Lettered footnotes follow tables.

Explanatory Notes to Tables 1-3

1. "State-owned enterprise" means wholly or majority-owned, unless information on ownership shares is unavailable. In several cases, we have counted as "state-owned" enterprises with slightly less than 50% public ownership.

The dates of liquidation refers to the post-1980 period, for most of the countries in Table 1. In some cases (Chile, Bangladesh, Pakistan, for example), the sales or liquidations/closures occurred earlier.

2. The data were obtained as follows: survey of published literature, and indications from previous research on privatization, provided an initial list of countries; project files in the World Bank were consulted for further leads. The Joint Bank-Fund Library and the Library of Congress were consulted; computer runs were made of the periodical literature and more specialized sources; World Bank reports on relevant countries were skimmed for any references to divestiture; staff of the World Bank, IMF, IFC, consulting firms and the Agency for International Development, and others were interviewed. The estimated numbers of liquidations and sales tend to miss one important category of divestiture: sales of equity owned by development banks and similar financial institutions. This is discussed in the text.

3. It is difficult to define "targeted" or "potential" divestitures precisely. Despite this, the concept has been retained in these tables to allow actual performance to be measured against some national goals. In each case, one of the following three definitions has been used to estimate the "target" or "potential" number of enterprises for divestiture:

- (i) decisions made by the government in question, as reflected in an official statement;
- (ii) recommendations and/or suggestions made by World Bank staff in reports focussed on SOEs;
- (iii) a combination of Government statements and agreements with the Bank under Structural Adjustment Loan or Credit Conditions or some other agreement.

Footnotes to Tables 1-3

Bangladesh

- (a) There were approximately 50 SOEs prior to the massive nationalizations that followed "liberation" in 1971. The total number of "abandoned" units was about 725, all of which were vested in the Government. Most of these were small. Later, 239 larger units were nationalized, leaving 484 still vested in the government. Therefore, the total number of enterprises is 392 or 778 depending on whether only the larger nationalized units included. (See S.H. Chrishty, "Privatization in Developing Countries: The Experience of Bangladesh," Conference on Privatization, Asian Development Bank, January 31-February 1, 1985, Manila, Philippines.)

- (b) These are entities divested up to 1983 and include units in the process of being divested, i.e. either on the auction block or advertised for buyers. The figure comes from R. Sobham and A. Ahsan, Divestment and Denationalization: Profile and Performance, draft paper, Dhaka, October 1983. Other estimates put the number at around 700. These differences probably revolve around treatment of the "vested" smaller units.

Brazil

The data came mainly from Walter Lee Ness, Jr., "Destatization Program of the Brazilian Government" n.d. (December 1984?).

- (a) There are nine "disactivated" firms, with 50 "in process."

Cameroon

Figures on the equity value of PE assets and the number of employees were World Bank estimates.

- (a) Among the five liquidated PEs are SIRICOM (brick manufacturing company), and SOCAME (fertilizers).
- (b) Government in April 1984 invited the Bank to assist in the study of public enterprises. The number of targeted divestitures comes from a prior World Bank study.
- (c) World Bank staff mention 6-10 management contracts but could provide specifics only on three: HAVECOM (rubber company), SUCUCOM (sugar company) and a shipping line.

Chile

Estimates for SOEs privatized after 1973 vary widely for reasons that are not clear. In his 1981 Journal of Development Economics article ("Towards a Free Market Economy"), Foxley gives 507 SOEs in 1973 and 70 in 1977. But CORFO figures (in Mary Shirley, Managing State-Owned Enterprises, p. 57) list only 133 enterprises sold from 1974 to 1982. The difference may be due mainly to whether "intervened" enterprises are counted or not; 259 firms were taken over this way in 1970-1973. The total value of 1974-82 sales, according to CORFO data, is \$940 million.

Dominican Republic

- (a) A foreign multinational, United Brands, leased 1,000 hectares from the State sugar company. It converted sugar land to pineapple and oil palm.

Ghana

In Ghana, a Working Group was established in May 1984 to oversee and coordinate a Bank-financed study of the public enterprises sector. The Bank study in Ghana was completed in August 1985.

Grenada

- (a) The only large hotel in Grenada, The Grenada Beach Hotel, was leased to a private developer who agreed to rehabilitate it. This would involve \$6-14 million in rehabilitation cost. Fifty rooms are expected to be added. It is a 99-year lease costing the developer \$50,000 a year or 1/4 of the profits, whichever is smaller.
- (b) The developer is giving a management contract to Ramada Inn International to manage it.

Guinea

- (a) The total number of enterprises will be 139 if individual gas stations and retail outlets are separately counted rather than included under one umbrella enterprise.
- (b) The 16 industrial enterprises no longer in operation included five that are closed but with some employees on payroll and 11 others that are in the process of being "renovated."
- (c) The number of enterprises to be divested was compiled by Inter-Ministerial Committee; it was not formally approved by the Government, as of April 1985. The 43 included 20 in the industrial sector, 2 in transportation and 21 in commerce.
- (d) There has been one lease--to Volvo--in the service industry.

Ivory Coast

- (a) The number of enterprises is sometimes quoted as 250. We use the latest figure, a 1983 World Bank estimate.
- (b) Even though a 1983 World Bank study mentions the closing down of 16 firms, we are able to identify only 10. These include BNEDD, AGRIPAC, ARSO, AVB, SCOFREL, SONAFI, Bureau Ivoirien de Normalisation, Center d'etail, Banque Ivoirienne de P. T. and Ivoire Outils.
- (c) This is a Government-initiated attempt to tackle the problem of public enterprises. Government efforts began in 1977-78.
- (d) Sales include IVOIROUTIL (a tool company), SUCATCI (a rubber company), SUNAGECI (construction company) and BNEC (a housing bank).
- (e) The three management contracts are: SODEPALM (palm oil processing company), PROCACI (primary processing of cocoa) and TRITURAF (soap manufacturing company).

Kenya

- (a) 1971-73.

Liberia

- (a) The number of "targeted" divestitures is from the Government of Liberia's structural adjustment program.

Malaysia

- (a) Two of the four privatized firms are partial privatizations. These are the AVIONICS Repair Facility and the Port Klang Container operation.

Mali

- (a) These include six small firms plus three larger ones: CMTR, Air Mail and SHM.
- (b) Potential divestitures come from the recommendations of a government-sanctioned study of the Public Enterprise Sector.
- (c) This includes Air Mali which has an arrangement with Air Afrique--the management of its international operations. There seems to be no equity transfer. The fate of Air Mali's local operations is, at the moment, not clear. Another is ITEMA--a textile company which was a joint venture--now further privatized with Malian shareholders.

Mauritania

- (a) Like most of the employment figures for the sector, this figure is highly suspect since it was based on a 1982 head count and therefore has a large error factor. One half of the sector's employment is for "Societe Nationale Industrielle et Miniere" (SNIM) which operates the iron ore mine.
- (b) The four liquidated or partially liquidated enterprises are: MAFCO (fishing); SMTM (hotel) which is closed with liquidation action underway; SOMIR (refinery) and Projet Sucre, whose refining unit is closed and whose processing plants are to be privatized.
- (c) The identification of the enterprises to be privatized was the result of a government study. The ten targeted enterprises are based on a World Bank sector study covering 30 enterprises.
- (d) The sale of ONC (cinema) was supposed to have been completed in 1984. We couldn't find out who bought it, or how much was paid.

Mexico

- (a) These are "empresas" (state enterprises) as of December 31, 1984, of which over 80% are majority owned. The state sector more broadly defined has 845 entities. In addition to the "empresas", there are 211 "Fidelcomisas" and 176 "decentralized organisms." This information comes from Revista de Administracion Publica, Empresa Publica #5960, July/December 1984, published by Instituto Nacional de Administracion Publica.

- (b) In 1983 and 1984. An additional 32 enterprises are to be liquidated in 1985. (*Ibid*, p. 164.)
- (c) This is also 1983 and 1984. An additional 44 SOEs are to be put up for sale in 1985. (*Ibid*, p. 164.)

Niger

- (a) The Conseil du Government of Niger decided during an October 4, 1984 meeting on the number of enterprises to be privatized. This included the sale of equity of nine public enterprises and the full privatization of 15 others. ("Privatization in Niger", Elliot Berg, consultant's report, December 1984.)

Pakistan

- (a) The number of public enterprises shown does not include the 2,000 cotton, rice and flour mills nationalized under the Nationalization Act of 1974; since these were denationalized less than a year later.
- (b) The six divested enterprises are two engineering firms, one sugar mill and three textile mills. In addition, 2,000 cotton ginning, rice husking and flour mills nationalized in 1977 under the Nationalization Act were returned to their previous owners in the same year.

Panama

- (a) "Targeted" divestitures sanctioned by the President of Panama in a televised speech on November 2, 1984. These include Air Panama, Cobana, Endema and Citricos de Chirique. One hotel has already been sold.
- (b) This was a major unprofitable hotel sold to a group of Japanese interests. Sale price was \$34 million. Cost to the Government had been \$54 million.

Peru

- (a) Estimated value of the 60-70 enterprises to be sold ranged from US\$400-600 million. This is equivalent to about 3% of Peru's GNP. ("Privatization of Public Enterprises in Peru: The Situation as of December 1981," IFC, April 1982.)
- (b) This is actually a case of partial privatization and succeeded in reducing the operation of PESCA-PERU, PEPESA and EPSEP. PESCA-PERU reduced employment from 6,000 to 1,200, PEPESA laid off 1,800 employees and EPSEP reduced its staff from 1,200 to 700.

Senegal

- (a) Employment figures are for about 75% of the total number of Government-owned enterprises. These include the relatively large enterprises.

- (b) Enterprises targeted to be divested are based on World Bank recommendations. These are mostly joint ventures with the Government owning minority shares.
- (c) The five privatized companies were previously mixed companies. They are SIV (textiles), SISCOMA (farm implements), IRANSENCO (petroleum distribution), SNCDS (tuna canning), SNTI (tomato canning) and SONAFOR (drilling of water holes).
- (d) These are mostly small manufacturing enterprises.

Sierra Leone

- (a) About ten years ago, the Sierra Leone railway was closed down.
- (b) The targeted number of enterprises to be divested is the Bank's recommendation.
- (c) The four leases are hotels.

Sri Lanka

Our data on Sri Lanka are based on a conference paper by Mr. I. Jayasinghe, "Privatization in Developing Countries: The Experience of Sri Lanka," Conference on Privatization, Asian Development Bank, January 31-February 1, 1985, Manila, Philippines, and a study by Marcia A. Wiss, "Divestiture of State-Owned Enterprises in Sri Lanka."

- (a) The 11 enterprises are an example of partial or quasi privatization in the sense that part of the shares were sold to the private sector with the State retaining majority ownership. These companies include SRMC (the State Rubber Manufacturing Corporation), four activities of the Cooperative Wholesale Establishment (CWE), Lanka Milk Foods Ltd., and the Department of Machinery and Equipment. (Conference, pp. 14-23.)
- (b) Five of the textile mills are under management contract (*Ibid.*, p. 13).

Sudan

World Bank files, February 1985.

- (a) Estimate.

Thailand

- (a) The two liquidated firms are Bankok Jute Mill and the Wire Diffusion Company.
- (b) The three privatized firms are: The Paper Factories of Industrial Workshop, Central Thai Industry Shop, Esarir Gunnybag Company, Ltd. Source: Business Review (Bangkok), March 1985 and P. Pakkasem, "Thailand," in Manila papers. There is ambiguity in these sources as to what has been sold and what liquidated.

- (c) Leasing--State Alum Factory.
- (d) There have been two joint ventures in Thailand within the last ten years. These are the Petroleum Authority which sells oil to the Government (1978) and the Airport Authority of Thailand (1979).

Togo

- (a) World Bank estimate.
- (b) One of the nine closures is in mining.
- (c) The choice of state enterprises to be divested was decided on by Government through a special ministry of State Enterprises called in Togo "la tutelle de la gestion."
- (d) Leases include SOTEXMA, the oil refinery and the recently leased steel mills (STS).
- (e) These are the four hotels.

Uganda

- (a) Of the 67 planned, 21 are planned joint-ventures, 15 to be sold or returned to former owners, and 31 to be sold or closed. Source: World Bank, Industrial Sector Paper, April 1985.

Zaire

- (a) The liquidations were: OZACAF (coffee marketing), CNECI (mortgage bank) and STK (urban transport).
- (b) The list of 37 enterprises to be privatized was the result of a 1982 Government study. Most of these were small farms, managed by the Ministry of Agriculture. A special inter-ministerial commission was set-up to implement the recommended action.
- (c) There are three agricultural marketing operations under Management Contract (1978). These are the palm oil, cocoa and tea operations.

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