

PUBLIC ENTERPRISES AS THE MAIN INSTRUMENT OF THE PUBLIC
SECTOR

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A. PRESENT ROLE AND SIGNIFICANCE OF PUBLIC ENTERPRISES

1. Universal spread of public enterprises

As instruments of public policy, public enterprises are now almost universal. Apart from their common use in centrally planned economies, they are widely used as such instruments both, in developed and developing market economy countries. This is true of Africa, Western Asia, Latin America and the Asian and Pacific regions.

Public enterprises are present within the major economic sectors in developing countries. They are most common for utilities, in transport and in manufacturing. In mining, public enterprises are especially important in such diverse countries as Brazil, Guyana, India, Iraq and Zambia. In manufacturing, they dominate in Iraq, Jordan, Morocco and Syria. In banking, public enterprises play an important and sometimes dominant role in Mexico, India, Pakistan and Uganda. In the tourist industry they run hotels and tour services, as in Jamaica and Thailand. State trading organizations dominate export and import trade in many countries and as for internal trade, they are used as effective instruments of public sector policy in India, Sri-Lanka, the Western African countries and some Latin American countries.

2. Quantitative dimension

Public enterprise sectors have grown and diversified greatly in the last two decades in most developing countries. As for the African region, parastatal sectors are larger in terms of GDP and investment than in other regions. An IMF study¹ has shown that while the percentage share of GDP at factor cost accounted for by public enterprises worldwide was 9.4% in 1974/77, the aggregate figure for all of the developing countries was 8.6% and that for Africa was 17.5%. As for the percentage share of gross fixed capital formation, it was 13.4% worldwide for the same period, 27% for the developing countries as a whole and 32.4% for the African region.

In the ESCAP region, there has been a marked growth in the number of public enterprises: in India the number increased from 5 in 1951 to 153 in 1978; in Malaysia, from 10 in 1951 to 701 in 1979; and in Indonesia, from 103 in 1960 to 168 in 1979.

As for the Latin American semi-industrialized countries, it can be mentioned that in Argentina there were 7250 companies included in the inventory of firms totally or partially owned by the State in the mid 1970s. They accounted for around 30% of all fixed investment in the country and were responsible for 45% of the external debt. By 1983, 65% of

1. Short, R. P.: "The role of public enterprises: an international statistical comparison", in R. H. Floyd et al, Public Enterprises in Mixed Economies: Some Macro-Economic Aspects, I.M.F., Washington D.C., 1984, pp. 126/129.

the capital represented by Brazil's 500 largest firms was state-owned, while only around 25% belonged to the country's private sector and 9% was foreign, mostly private capital; regarding their numbers, public enterprises grew from about 49 in 1950 to about 560 in 1980. Parastatals in Mexico account for 100% of the production and distribution of energy, 100% of air and railroad transportation and of communications, produce more than 60% of the steel and 15% of manufactures and since 1982 include all of the banking services².

3. Public enterprises as instruments of public policy

As instruments of the public sector, public enterprises are used in a wide variety of policy areas, from managing the economy and regulating economic behavior to production. The objectives and "strategic missions" assigned to them (formally or informally) in developing countries include to generate employment, control and/or manage strategic sectors of the economy, control monopolies, promote regional development, provide the basic infrastructure required for development, substitute imports and/or save foreign exchange, implement economic policies and/or plans, earn profits for investment elsewhere, provide traditional public services, counterbalance the power of domestic entrepreneurs and/or multinational enterprises, regulate markets, reduce income inequalities, prevent private business failures,

2. Eisenstein, Jorge: La gestión de empresas públicas en México, CIDE, Mexico, 1983, pp. 75 and 182.

overcome obstacles to economic development, avoid denationalization of local enterprises, enter into joint ventures with foreign capital, increase production, enhance national prestige, and ideological commitment³.

B. CURRENT ISSUES AND CONCERNS ABOUT THEIR ROLE

Given the importance of the public enterprise sector and the scale attained by State entrepreneurship in most developing countries, it comes as no surprise to find that almost no country has been spared what appears to be a permanent debate about the role of public enterprises in economic development, their relationship with the private sector, their performance, the institutional arrangements under which they function and how to ensure that they operate efficiently. The issues at stake are grouped below in three clusters.

1. Public enterprise deficits and the fiscal crisis

In the 1960s and 1970s, the debate mentioned before and the initiatives for reforms focused mainly on the control, organization, management and accountability of public enterprises. In the 1980s, the losses and inefficiencies of many public enterprises are widely viewed as a contributory factor to the economic malaise in developing countries. There is substantial evidence to believe that the overall profitability (meaning return on total capital employed i.e.

3. Adapted from Barenstein, Jorge: *op. cit.*

gross fixed investment minus depreciation plus working capital) of the parastatal sector in various regions of the world is largely negative⁴. Undoubtedly, there are many bright cases but, in most individual countries, the return on the overall portfolio of investment is negative.

The scenario is further complicated by developments in the international commodity and financial markets, that forced many developing countries to adopt policies of adjustment that have, among other things, called for fiscal retrenchment and for reducing the public sector borrowing requirements. No less urgent is the adoption of policies aimed at restructuring production so as to expand capacity to export manufactures and semi-manufactures.

2. Rethinking the role of the public sector

The scenario of crisis depicted above had a tremendous impact on the approach of governments to the problems of their public enterprise sectors. The economic crisis of the 1980s may prove, in fact, to be a historical watershed in the re-orientation of the role of the public sector in many developing countries.

The crisis has been the main cause for the frequent cases of rethinking and redesigning of policy that resulted in the questioning of the traditional role of public enterprise and, more broadly, of that of the State.

4. Short, R. P.: *op. cit.*, pp. 146-149 and 151-158.

3. Rethinking the institutional arrangements for government direction, control and evaluation

As a result of their rapid growth and of the elusive nature of their assumed public purpose (as compared to private profit), a variety of constraints - and additional costs - on the operations of public enterprises have appeared. They include such planning, direction, organization and control failures as poor feasibility appraisal and decisions about initial investments, poor corporate planning, little incentives for entrepreneurial behaviour, inability to generate income to maintain operations, inadequate arrangements for accountability, and trivialization of board and political supervision.

The above reported state of affairs results also from the fact that public enterprises are frequently subject to a diversity of control and direction from other government agencies, that often have conflicting priorities, what have resulted in costly delays and inefficiency in the enterprises affected by those controls.

C. PUBLIC ENTERPRISE REFORM: RECENT EFFORTS

A number of developing countries have contemplated or implemented in the 1980s wide-ranging public enterprise reforms, divestment and liquidations. This chapter will make reference to some of their most salient aspects.

1. Institutional aspects

Several institutional arrangements have been used in developing countries to provide control and supervision of public enterprises. In some countries they are under the oversight of sectoral ministries to which they are assigned; in others there is, in addition, a central bureau that collects and analyses information about them and often performs other functions; in still others, control is vested in a standing congressional committee; sometimes supervising authority is removed from ministries and vested in a holding company; there is also the control and supervision provided by presenting reports and accounts of enterprises by the auditor general before the legislature; and finally, the most recent approach to the problem of malfunctioning institutional structures in some countries has been the creation of "focal points", to oversee the public enterprises.

The different alternatives mentioned above were enforced attempting to keep a clear distinction between policy formulation, control and evaluation, on the one hand, and the management of public enterprises on the other. In many cases, they have nevertheless failed in providing the necessary degree of autonomy for effective management.

2. Divestment policies

Taking Africa as an example, it can be seen that Nigeria has liquidated its marketing boards and Cote d'Ivoire, Kenya and Morocco are among the countries which have divested (or "privatized") some public enterprises. This has indeed emerged as a phenomenon of our times and the pendulum seems to be swinging, in many developing countries, in the direction of the moderation of the interventionist impulses of the State. Divestment policies however, have usually been hampered by gruelling problems, as will be commented below.

Firstly, the proper valuation of enterprise assets prior to the sale and the timing of this activities, constitute a very tricky undertaking. Secondly, divestment requires a capital market to exist in the country and, should that be the case, it also requires a sophisticated infrastructure of banks or investment brokers, to provide outlets for shares and broader participation, all of which is hardly the case in most developing countries.

In the third place, divestment can leave a vacuum regarding the role that public enterprises have as instruments of public policy. In some cases, it became thus necessary after divestiture, to create a new institutional framework for monitoring developments in the affected sectors of activity, so as to ensure that public policy objectives were met. And finally, there must be widespread political support for the rationale of divestment: particularly in the case of enterprises with a strategic role in the national economy,

it is not enough to proceed on the basis that the activity could just as well be undertaken by the private sector. Political reality often requires difficult and costly efforts to explain the measures to be taken and to obtain support for their implementation.

3. Improving managerial performance and control

In countries with mixed economies, the measures adopted to raise internal efficiency in the parastatals are frequently oriented towards having them follow market signals more closely and be subject to the discipline of the market. Consequently, in several countries, public enterprises have to recourse to borrowing in the financial markets rather than depending on the Treasury, prices have been raised and tax exemptions have been revised.

Efficiency in public enterprises is also being raised by the adoption of new and better managerial tools. Foremost among them are management information, monitoring and performance evaluation systems. The best among those systems are kept simple and go from collection of detailed data (to suit the individual operating units' needs) to different degrees of aggregation (to suit the needs of the various planning, oversight and controlling agencies).

Training is widely viewed -together with appropriate salary and career planning policies- as a basic solution for improving managerial capabilities in the parastatal sector. Training programs are beginning to be designed considering

the specific needs and characteristics of top managers of the public enterprises and high level officials of the various oversight and planning agencies concerned with them.

Finally, and regarding managerial performance on the job, reform efforts point to the ways for strengthening accountability and responsibility for results. A key factor here is managerial motivation, that is to say, how to relate closely the managers' incentives (both monetary and non-monetary) to their enterprises' performances. "Contract programmes" are among the techniques being tried to that effect.

4. Emerging trends

In some countries, mainly due to the economic crisis, a new configuration seems to be emerging in their development policies, to the extent that market institutions have been fleshed out and private entrepreneurship and managerial experience have built up. In those cases, the belief has spread that there is now less call than hitherto for the State to act as catalyst and market surrogate. There, some form of divestment in favor of mixed or private enterprises is being sought. But the aforementioned requisites prevail in but a handful of developing countries... For the most general case, there are reasons to suppose that public enterprises will continue to figure prominently on the economic scene for a good many years to come, albeit with a

tightened management and greater exposure to the discipline of the market.