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PRIVATE SECTOR DEVELOPMENT AND PRIVATIZATION IN DEVELOPING COUNTRIES:

TRENDS, POLICIES AND PROSPECTS

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PREFACE

This study on private-sector development and privatization in developing countries was carried out by the Industrial Development Review Unit, Programme Support and Monitoring Branch, UNIDO, within the framework of its work programme on policy-oriented research studies. It is based on the recognition that private-sector development is being given increasing priority throughout the world, from the former centrally-planned socialist economies of central and eastern Europe and the Commonwealth of Independent States (CIS) to most developing countries and industrialized economies. This increased emphasis on the private-sector development represents a response both to the relatively poor performance of most state-owned enterprises (SOEs) and the increasingly tight budgetary constraints faced by many governments, which prevent them from providing the subsidies and other forms of financial support that these SOEs often depend upon for the survival. Consequently, the privatization process has become an important, and inevitable, corollary of this increased emphasis on private-sector development.

The main purpose of this paper is to review the experience and effects of the privatization process to date, and from this analysis to draw conclusions about the prospects for further privatization in the 1990s. The scope of the study is confined mainly to the experience of developing countries in privatization and private-sector development, with marginal references to east and central European countries where appropriate.

The present study comprises seven Chapters. Chapter I introduces the scope and methodology of the study. Chapter II reviews the principal policy issues relating to various stages of privatization, including an assessment of the need for enterprise restructuring prior to privatization, together with the extent and magnitude of privatization and likely trends in various industrial subsectors; alternative techniques applied, including foreign participation and the sequencing of privatization programmes. Chapters III, IV and V deal with country experience of privatization in the three principal developing regions of Latin America, Asia and Africa, respectively, together with trends and impact on industrial production and technological development. Chapter VI presents an overall assessment of privatization strategies and policies that were adopted in these countries and regions and their socio-economic implications, highlighting the need for a combination of privatization with appropriate economic and industrial policies to promote private-sector development. The institutional requirements for privatization are also examined, together with the legal, financial, managerial and technical expertise necessary for successful implementation, with a focus on the prospects for privatization in developing countries in the 1990s. Chapter VII discusses the potential role of international agencies, particularly UNIDO, in developing a suitable environment for private-sector industrial investments and in assisting the process of privatization in industrial subsectors and industry-related services in developing countries.

The study was prepared by Professor Katherin Marton, Fordham University, New York, as UNIDO consultant, and finalized by the Industrial Development Review Unit of UNIDO.

EXPLANATORY NOTES

The following abbreviations are used in this document:

APT	Asset Privatization Trust
ASEAN	Association of South-East Asian Nations
CIS	Commonwealth of Independent States
COP	Committee on Privatization
FDI	Foreign direct investment
GDP	Gross domestic product
GNP	Gross national product
SOE	State-owned enterprise
TNCs	Transnational corporations

SUMMARY

Introduction

This study reviews the experience and trends in privatization of state-owned enterprises (SOEs) in various industrial subsectors and industry-related services in developing countries and examines the magnitude, implications and issues relating to privatization. These include the objectives of privatization; the different methods used; the preparation and sequencing of privatization programmes including assessment of the need for enterprise restructuring; the role of local capital markets and foreign investments, and policies and institutional requirements for privatization within the broader framework of private-sector development in these countries. The experience of privatization in the Latin American, Asian and African regions has been analyzed, together with assessment of the broad impact of privatization on national economies and prospects for further privatization in these regions during the 1990s. Among developing countries, privatization has been most extensive in Latin America, though there have been a large number of privatizations in Asian and African countries also. Privatization has taken place in various industrial subsectors, besides infrastructure and industry-related sectors such as mining, and various service sectors. In several countries, there have been relatively few cases in the manufacturing subsector, largely because of the strong presence of private-sector industrial enterprises. The study concentrates on experience of privatization in Latin America and the Caribbean, Asia and Africa.

Issues and trends

There has been a considerable increase in privatization in developing countries in recent years. By 1992, about 80 countries had adopted privatization programmes and, during the period 1980-1991, there were 1,357 cases of privatization in developing countries. Most of the privatizations took place in Latin America (804, constituting over 59 per cent), followed by African countries (373, constituting 27.5 per cent). In Asian countries, there were only 122 cases (9 per cent) during this period, with the remaining cases in the Middle East and North Africa. These numbers have, however, to be interpreted with care, since several cases, particularly in Africa, relate to very small enterprises. The issues relating to privatization in these countries differ considerably from those in industrialized countries and in former centrally-planned economies. In industrialized countries, the objectives are primarily to achieve greater efficiency and competitiveness within the framework of an efficient capital market and strong private-sector response. In former centrally-planned economies, privatization of enterprises is part of a more comprehensive shift to a market economy. Developing countries often provide a mix of the two, with local capital markets and private-sector response varying from country to country. While these have been fairly adequate in several Latin American and Asian countries, they are very inadequate in most African countries and in the least developed economies. Several factors are involved in the determination of an appropriate strategy for privatization in developing countries. These relate to the objectives sought to be achieved, which can range from single to multiple goals; the techniques of privatization; the nature of ownership transfer; subsectoral trends; and the sequencing of privatization.

Objectives

The objectives of privatization in most developing countries have been of a multiple nature. In certain countries, particularly in Latin America, relief from heavy foreign debts was an important objective. Other major objectives comprised reduction of financial burden on account of losses and subsidies, and funds for investments; income from sale of assets or shares of SOEs; increase in efficiency and competitiveness of privatized enterprises; distribution of ownership, and enhancement of private-sector development.

Techniques of privatization

These range from sale of shares of SOEs through private placement or public offering; sale of newly-issued stock; restructuring of the enterprises and sale of only a part of the company; sale

of stock to management or employment; leasing or management contracts, or liquidation and sale of assets. In Latin American countries, as also in some Asian countries, the local stock exchange has often been used in combination with private placement. In most Asian countries, however, public offerings tend to be more common. In several countries, particularly in Africa, a number of small SOEs have been liquidated and closed down.

Ownership transfer

An important issue is whether full or partial ownership is to be transferred and if such transfer is to be confined to local investors. In most developing countries, ownership transfer has been primarily to local investors though in certain fields such as telecommunications and airlines, besides hotels, the participation of foreign partners has been encouraged. In several Latin American countries, foreign investment participation has also taken place through debt-equity conversion arrangements, though the major initiative was taken by private-sector groups in these countries. In most Asian countries, the participation of foreign capital has been less pronounced, except in the Philippines, and most of the capital has been raised by local shareholders.

Subsectoral trends

In the manufacturing sector, privatization has extended to textiles and sugar plants in the Philippines, petrochemicals in Argentina, steel production in Brazil, Mexico, Chile, the Republic of Korea and Taiwan Province of China. Several industrial were enterprises privatized in Pakistan during 1991-1992. Privatization has also been extended to several non-manufacturing fields including power utilities in Chile, Argentina and Philippines; mining enterprises in Chile and Mexico; telecommunications in Chile, Argentina, Malaysia and the Republic of Korea; airlines in Argentina, Chile, Mexico, Malaysia, Singapore and the Philippines; and banks and financial services in Chile, Uruguay and the Philippines. These privatizations have been quite successful in terms of transfer of ownership, though it is still too early to assess their impact on efficiency and increased technological competitiveness. In African countries, most of the state enterprises privatized were relatively small production or commercial units, in various fields. Their privatization has had little impact so far, apart from reducing the financial burden on governments.

Sequencing

A critical aspect of privatization strategy is the sequencing of privatization activities, both in terms of sectoral priorities and various stages of pre-privatization preparation and restructuring. These include determination of objectives and sectoral priorities; selection of enterprises; restructuring of enterprise, legal, financial and industrial; valuation of enterprises, or parts thereof to be privatized; preparation of enterprise profile and prospectus; determination of price and conditions of sale or allotment; selection of prospective investors; and, finally, approval of the privatization transaction. In most privatizations in developing countries, sequencing has been done with care, though there have been relatively few cases of pre-privatization restructuring of enterprises.

Privatization in Latin America and the Caribbean

Among developing regions, the most extensive privatization programme took place in Latin America, largely during 1988-92. By 1992, gross proceeds from privatization rose to over $50 billion, with the highest income for Mexico ($30 billion), followed by Argentina ($9.9 billion); Brazil ($4 billion); Chile ($3.4 billion); Venezuela ($2.1 billion) and the balance to other countries in Latin America and the Caribbean. The most comprehensive programme was undertaken in Chile, covering the steel and chemical sectors; banks and financial services; power utilities; telecommunications and airlines. In Mexico, privatization was extended to banks; mining enterprises; iron and steel companies; fertilizer plants; airlines and telecommunications. In Argentina, privatization was implemented in power utilities; telecommunications; petroleum and gas operations; airlines; and other production and service sectors. In Brazil, privatization has been largely concentrated in iron and steel and in fertilizers. Privatization in Venezuela was extended to airlines; banks; and telecommunications. Privatization was also undertaken in Honduras (airlines); Uruguay (banks); Peru (banks; airlines and iron and steel); Guatemala (airlines); Costa

Rica (fertilizers); Colombia (hotels); Jamaica (telecommunications; banks and hotels); and Trinidad and Tobago (fertilizers).

Various methods were used for privatization, including liquidation of SOEs and sale of assets; considerable use of local stock exchanges and, in some cases, foreign stock exchanges; allocations of shareholdings, including to local and foreign investors and to workers. A major role was played by domestic investor groups, though there was considerable foreign participation in privatized enterprises in telecommunications, airlines and hotels. In most countries, privatization proceeded fairly smoothly and rapidly and local capital markets were able to absorb the volume of shareholdings issued. At the same time, since there was little restructuring prior to privatizations, most of the enterprises were sold on an as is basis though, in some cases, privatization was separately conducted for different plants of the same enterprise. Despite the rapid pace of privatization in certain countries and subsectors, the impact of privatization has been quite positive, in that international debt burdens and financial burden of SOEs have been substantially reduced and policies of liberalization and deregulation, which have accompanied privatization, have resulted in increased flow of FDI and enhancement of private-sector investments. At the micro level also, there has been increased investment and improved technological and managerial impact on privatized enterprises. At the same time, there has been considerable retrenchment of workers and price of services of privatized enterprises have risen considerably, pointing to the need for regulatory measures in the post-privatization stage, particularly where monopoly operations are involved.

Privatization in Asian developing countries

Privatization has increased considerably in several Asian countries in recent years, although the number of enterprises and volume of transactions is much lower than in Latin America. The objectives were also of a multiple nature, as in the case of Latin American countries, though in the Republic of Korea, Taiwan Province of China and Singapore, one objective was also to avoid competition with the private sector. In several countries in South-East Asia and in West Asia, the private sector is already dominant in various industrial subsectors, with SOEs largely concentrated in infrastructure and in basic industries, particularly steel and petroleum, and petroleum-related industries. Major programmes for privatization have been undertaken in Malaysia (telecommunications, airlines, container terminal, etc.); the Republic of Korea (power utilities, steel); Taiwan Province of China (steel, banking); Singapore (telecommunications, airlines); Bangladesh (manufacturing and services); Pakistan (manufacturing units, banks, and services) and Sri Lanka (manufacturing units). A beginning has also been made in India, with partial privatization of selected SOEs, but channelled through the state-owned Unit Trust. The process of privatization has been much more gradual than in Latin America. Most of the privatizations have been conducted through stock exchanges and public offerings, with the shares being purchased by domestic investors. Unlike certain Latin American countries, however, where sale of shares was often to local core industrial groups, most share offerings in Asian countries had wider distribution of shareholding. The local capital markets have been able to absorb the holdings issued, partly because the sale of shares of major undertakings particularly in the Republic of Korea, Malaysia and Singapore was spread over a period of time. In Asian countries also, the impact of privatization has generally been quite favourable, both with respect to reduction of financial burdens of SOEs and enhancement of the role of the private sector in respective countries.

Privatization in African developing countries

However, in terms of numbers, privatization in African countries has been greater than in Asian countries, a large number of the cases involved were very small enterprises and total proceeds from privatization have been relatively low, with the exception of Nigeria. Most divestments have occurred in manufacturing and services, with the principal objective being to reduce the financial burden of SOEs. The Structural Adjustment Programme of the World Bank, which was extended to about 30 countries, placed considerable emphasis on reform of SOEs, both through liquidation of inefficient enterprises and privatization of others. The countries which undertook privatization programmes included Nigeria, Togo, Côte d'Ivoire, Gambia, Ghana, Guinea, Senegal and Niger, besides Tunisia and Morocco in North Africa. Divestments have also taken place in Liberia, Malawi, Mali, Mozambique and Zaire. Plans for privatization have also been initiated in Kenya and are planned in Egypt. Privatization was accompanied by liberalization and deregulation, with greater emphasis on private-sector participation. The most extensive programme for privatization was taken up in Nigeria during 1989-92, which included 51 SOEs engaged in cement, sugar, food, textiles, woodworking, engineering, paper and fertilizers. In 1993, 5 per cent of the Nigerian National Petroleum Company, was divested. In Côte d'Ivoire, 28 parastatal enterprises were privatized by 1992, in various manufacturing and service sectors, including power utilities. In Ghana, 49 privatizations took place by 1992 and several small enterprises were closed. In Mozambique, 216 companies have been privatized since 1987, including over 150 small and medium companies. In Senegal, 15 SOEs are in different stages of privatization, while 18 SOEs were privatized in Togo by 1990; 4 in Mali, 9 in Zaire; and 21 SOEs in Zambia by 1992-93. In Tunisia, 15 SOEs were privatized in 1989, besides 5 hotels sold to private buyers. In Gambia, 10 privatizations were completed by 1989, including in manufacturing and services, and in Guinea, 43 SOEs were planned to be privatized. In several cases, privatization was undertaken through local stock exchanges, as in Nigeria, Côte d'Ivoire and Kenya, and in Tunisia, but most of the SOEs were either liquidated or sold directly to private buyers. Privatization has resulted in limited foreign investments in certain countries such as Kenya, Côte d'Ivoire, Guinea, and Togo.

An assessment

There can be no doubt that a substantial level of privatization has taken place in a number of developing countries. This has been particularly effective in several Latin American countries, where it has had major impact in certain countries such as Chile, Mexico and Argentina and in several industrial subsectors such as steel, fertilizers, petrochemicals and other manufacturing fields, besides in infrastructure sectors such as power utilities, telecommunications and transportation, including airlines, as well as industry-related services. At the same time, there have been growing socio-political implications and effects. This has included criticism relating to retrenchment of labour consequent on privatization; prices received for privatized enterprises which are alleged to be too low, and prices charged for services of privatized enterprises. There have been considerable variations in the methods used. While, in Latin America, there has been greater emphasis on local core industrial groups which have taken the major lead, in most Asian countries, there has been wider distribution of shareholding. Ownership transfer has mostly been to local industrial groups and shareholders, with foreign participation in Latin America and Asia being largely limited to certain sectors such as telecommunications and power utilities, and in mining, besides services such as airlines and hotels in Latin American and Asian countries and over a broader range in certain African countries. On the whole, the impact of privatization has been positive in most developing countries in that the financial burden of SOEs has been substantially reduced, together with international debt burden of several countries. There has also been increased investment and introduction of modern technologies and management in privatized enterprises, though price of services has often increased. Since privatization has been accompanied by deregulation and liberalization of industrial policies, there has been a major fillip for private-sector development.

Prospects for privatization in the 1990s

Despite the fairly extensive privatization programmes undertaken up to 1993, there continue to be considerable prospects for further privatization in developing countries during the 1990s. In Latin America, such potential exists particularly in Brazil, but also in Mexico and Argentina and in a number of countries such as Bolivia, Columbia, Peru, Panama and Uruguay, besides Central American and Caribbean economies. In Asia, major potential for privatization exists in India, Indonesia, Iran, as well as some West Asian and South-East Asian economies where a number of SOEs continue to operate. In African countries also, with increased emphasis on private-sector growth, there continues to be considerable potential for privatization in several infrastructure and industry-related fields.

Role of international organizations, particularly UNIDO

International agencies, particularly UNIDO, can play a major role in assisting developing countries in privatization. The principal initiative in this regard has been taken by the World Bank, whose activities in this field will continue to be of major importance. At the same time, UNIDO can concentrate on privatization activities relating to the industrial sector and industry-related services and can provide a detailed range of services for this purpose. Such services can extend to policies, institutional support subsector programmes and enterprise-level assistance on various aspects of privatization, both during the pre-privatization stage and in relation to specific needs in particular subsectors. UNIDO's advisory activities relating to privatization would need to be considered both for the economy as a whole and in relation to specific enterprises to be privatized. Such assistance will be particularly valuable for developing countries in determining the scope for privatization; the criteria to be followed; the need for enterprise restructuring; the principles governing valuation of assets and assessment of viability; determination of the modalities for privatization; and assessment of final results. UNIDO can also play a useful role during the post-privatization stage by providing contacts and linkages with foreign enterprises and the development of suitable technological and marketing relationships with such enterprises.

CONTENTS

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I. INTRODUCTION

This study concentrates on the strategies, experience and potential for privatization in developing countries, with special reference to the industrial sector as well as industry-related infrastructure and service enterprises. It contains a comparative review of privatization in the developing regions of Africa, Asia, Latin America and the Caribbean and of the experience and impact of privatization in different sectors in these countries. An analysis is made of the principal issues pertaining to privatization, particularly of state-owned industrial enterprises and of the policies and measures necessary at the pre-privatization stage and in the course of privatization, as also during the post-privatization period.

The global trends towards increased private-sector orientation are reflected in the privatization and divestment of government holdings in a wide range of industrial enterprises, including basic production sectors, such as steel, mining, and petroleum-related industries, as well as in infrastructure and service sectors such as power utilities, and telecommunications, besides airlines and hotels. The pattern has varied considerably in different countries, but there is a marked shift to private-sector development in most economies. The nature and extent of privatization has also varied from country to country and is obviously related to the extent to which industrial and commercial functions and services had earlier been undertaken or taken over through state-owned entities. In most industrialized countries, particularly in Europe, privatization in recent years has extended to industrial, mining and infrastructure sectors in certain countries and can be expected to be extended to similar enterprises in other European countries, where substantial governmental investments have been made in such enterprises. In the former centrally-planned socialist economies, privatization is being rapidly extended to most economic activities and inevitably has very wide and comprehensive application. The privatization of industrial enterprises and infrastructure entities in these countries is, however, likely to be a fairly gradual process, in the absence of local capital markets and with limited private-sector resources and initiatives, and would depend, to a large extent, on foreign direct investments and participation.

In developing countries, policies with respect to private-sector industry and privatization largely reflect historical developments, on the one hand, and response to changing, contemporary socio-economic and technological developments, on the other. The period of the 1960s and 1970s was a period of major state interventions in ownership of industry, mining and services, apart from infrastructure, in most developing countries, with state-owned enterprises playing an increasingly prominent role in various priority sectors. At the same time, in most developing countries where significant levels of industrialization have been achieved, the private sector has also played an important role, specially in manufacturing, and mixed economies emerged, comprising both state-owned and private-sector enterprises. Since the latter half of the 1980s, however, inadequate economic performance of state-owned enterprises, combined with the deteriorating economic situation and the heavy debt burden in several developing countries, has resulted in much greater emphasis on private-sector development, and consequently on privatization of public-sector enterprises.

The concept of privatization in industry essentially involves the transfer of ownership and full or partial divestment of government holdings in state-owned entities and industrial enterprises to the private sector. Privatization has assumed a major dimension in several developing countries and constitutes a vital aspect of industrial restructuring and development of international competitive capability in these countries.

The need for the privatization of state-owned industrial and industry-related enterprises has, in general, been recognized in most developing countries as an integral element in the growing emphasis on private-sector development and on market forces rather than on the government, both for allocation of resources and for production and distribution in various fields. There has been increasing dissatisfaction, particularly with the economic performance of state-owned industrial enterprises, which have often continued to depend on subsidies from their respective governments to finance operating losses in a large number of cases, apart from their dependence on governments for new investments. In several developing countries, state-owned enterprises have also been major borrowers of foreign capital and have contributed to rising external indebtedness.

The growing trend towards privatization and its increasing acceptance in most developing countries during the latter half of the 1980s and early 1990s, has been influenced by several factors. Firstly, the continuing losses or low earnings of most state-owned industrial enterprises and their need for subsidies and financial support have contributed significantly to budget deficits which, together with the high external debts in many of these countries, necessitated the imposition of strict budgetary policies. It has become increasingly necessary to reduce the financial burden of state-owned enterprises, on the one hand, and to augment revenues from the sale and disposal of state-owned assets, on the other. Secondly, with the major shift in economic and industrial strategies in most developing countries towards free-market economies and increased emphasis on the private sector for industrial growth, the privatization of state-owned enterprises constitutes an essential element. Thirdly, there has also been growing recognition of the need to move from import-substitution to export-promotion development strategies. Since promotion of exports requires competitiveness of local industrial enterprises, both in international and domestic markets, and the development of necessary infrastructure and services for this purpose, there is much greater need for inflows of foreign capital and participation, including new and modern technologies and managerial expertise. Consequently, developing countries adopting privatization programmes have also undertaken a significant liberalization of their economy, including deregulation of industrial controls and markets and of international trade, and promotion of foreign direct investment and technology inflow. These macro-economic policy changes and adjustments were also encouraged and, in certain cases, insisted on by international lending institutions as part of Structural Adjustment Programmes and as a condition for debt restructuring of highly-indebted countries. Privatization in most developing countries has, therefore, been part of a comprehensive economic policy package for liberalization and deregulation.

II. PRIVATIZATION IN DEVELOPING COUNTRIES AND REGIONS

A. BACKGROUND: ISSUES AND APPROACHES ACROSS REGIONS

By the end of the 1970s, the role of state-owned enterprises in developing countries had increased considerably and the share of such enterprises in GDP and in gross fixed capital formation was quite significant. Such enterprises occupied a dominating position in several developing countries, ranging from 90 per cent of GDP in Algeria to 15-40 per cent in a number of other countries. Table II.1 indicates the size of the public-enterprise sector in the late 1970s to early 1980s, before privatization programmes had been adopted in most of the countries. The role of state-owned enterprises in various sectors of the economy is presented in Appendix 1.

Since the latter half of the 1980s, the combination of unsatisfactory economic performance of state-owned enterprises, and the deteriorating economic situation and pronounced shift towards private-sector development, has resulted in varying degrees of privatization in a number of developing countries. The range and magnitude of privatization of state-owned enterprises (SOEs) in developing countries has increased considerably, particularly during the latter half of the 1980s, and continued to grow during 1990-1993.

The basic issues relating to privatization in developing countries differ considerably from those relating to privatization in industrialized economies such as Great Britain or France and from those in former centrally-planned economies in Central and Eastern Europe and in the former Soviet Union. In industrialized countries, divestment of government holdings has been undertaken for financial reasons but primarily to increase the output, management efficiency and competitiveness of such enterprises and to distribute ownership of such enterprises over a much wider base to private-sector groups and individuals. Privatization is, however, undertaken within an overall economic environment of strong financial markets, stock exchanges and financial service institutions and substantial private-sector initiatives for investment and participation. In the case of the former centrally-planned economies, the need for privatization is part of an overall process of rapid shift to market economies and private-sector development. At the same time, there is also immediate need for restructuring of industrial enterprises in most of these countries, because of the deteriorating conditions under which such enterprises have been functioning, including inadequate product development, obsolete equipment and technological practices, poor management and marketing skills, and non-competitive capability, combined with lack of resources and inadequate institutional support for new investments.

The operating conditions of state-owned enterprises in industry, infrastructure and industry-related sectors in developing countries vary considerably and cover a wide range, both in terms of enterprise-level performance and the overall climate for privatization. Where such enterprises are modelled on the lines of enterprises in former centrally-planned economies, as in the case of Egypt, India and certain other developing economies, the problems may be similar to those in these economies. In state-owned enterprises following commercial policies and objectives, performance has generally not been satisfactory, or has yielded very inadequate returns even for enterprises producing or supplying products and services on a monopoly or semi-monopoly basis, as in steel, petrochemicals, fertilizers and machinery industries, or services such as telecommunications, hotels, and transportation. This has been combined with an overall environment in a number of developing countries, where the role of the private sector was, in the past, largely regulated and controlled, including levels of production and prices, and where the necessary infrastructure for successful privatization in terms of local capital markets, stock exchanges and financial institutions is often not in place. The climate and infrastructure for privatization in developing countries can vary considerably. In general, the more industrialized a country may be, the more likely is the availability of the requisite infrastructure for privatization. In several Latin American and Asian countries, local capital markets and financial and other institutions, together with private-sector participation is available to a fairly adequate extent, to meet privatization needs. This is not, however, the case in most African developing countries, as also in several industrially less-developed economies in Asia, Latin America and the Caribbean.

Table II.1. Size of the public enterprise sector in selected developing countries, selected years and periods

Region, country or area	Share of public enterprises in GDP or GNP (Percentage)	Year	Share of public enterprises in total gross fixed capital formation (Percentage)
Africa			
Algeria	90	1987	68
Benin[a/]	8	end-1970s	-
Botswana	7.3	1978-1979	7.7
Côte d'Ivoire	10.5	1979	39.5
Ghana	36.5	1983	28.7
Guinea	25.0	1979	-
Kenya	8.1	1970-1973	17.3
Liberia	6.8	1977	14.1
Mali[a/]	10	end-1970s	-
Morocco	19.7	1982	28.1
Niger	10.0	1979	39.5
Senegal	19.9	1974	17.9
Sierra Leone	7.6	1979	19.6
Sudan	40.0	1975	-
Togo	11.8	1980	-
Tunisia	24	1984	40.4
United Republic of Tanzania	12.3	1974-1977	32.7
Zambia	37.8	1979-1980	61.2
Asia			
Bangladesh	3.2	1984-1985	20
India[a/]	10	end-1970s	33
Nepal	3	end-1970s	-
Pakistan[a/]	8	end-1970s	45
Philippines	3.3	1983	22.4
Republic of Korea	9	1981-1983	23
Latin America			
Argentina[a/]	5	..	-
Bolivia	17.3	1980-1982	68.4
Chile	12.3	1982-1984	24.5
Jamaica	21	1984	42
Mexico	18.2	1983	25.5
Paraguay[a/]	3	end-1970s	-
Venezuela	27	end-1970s	36

Sources: Based on John R. Nellis, *Public Enterprises in Sub-Saharan Africa,* World Bank Discussion Paper No. 1 (Washington, D.C., World Bank, 1986), pp. 7 and 9; O. Bouin and Ch.-A. Michalet, *Rebalancing the Public and Private Sectors: Developing Country Experience* (Paris, OECD, 1991), pp. 64-65; *World Development Report 1983* (Washington, D.C., World Bank, 1983), pp. 49-51; Hacene Boukaraoun, "The privatization process in Algeria", *The Developing Economies,* vol. XXIX, No. 2 (June 1989), p. 112; and Young C. Park, "Evaluating the performance of Korea's government-invested enterprises", *Finance and Development,* vol. 24, No. 2 (June 1987), p. 25.

a/ Approximate figure.

There are considerable differences in the approaches and methodology adopted for the implementation of privatization or divestment programmes in developing countries, as compared to industrialized economies. These differences relate to the criteria for selection of subsectors and enterprises; the techniques and methodology for privatization, and alternative approaches for mobilization of financial resources. On all these aspects, the privatization process can vary considerably between developing and industrialized countries and between developing countries and former centrally-planned economies. The selection of subsectors and enterprises in industrialized countries relate largely to infrastructure and services, comprising telecommunications, power utilities, airlines, port facilities and other such enterprises. This is primarily because there are few industrial enterprises which are state-owned with the exception of certain basic industries such as steel or petroleum-related production and sectors such as mining. In France, however, such enterprises include production of aluminium, automobiles, and aerospace products, while in Italy, a number of state-owned industries are operating in chemicals, fertilizers and petrochemicals and in other fields. In the case of former centrally-planned economies, all enterprises were formerly state-owned and the selection of subsectors and enterprises to be privatized is often determined by private-sector response, including foreign companies willing to invest in, or to take over, such enterprises. In most developing countries, however, there is a fairly wide range of state-owned enterprises which deal with industry or industry-related services and selection has to be made of the specific enterprises to be privatized. With respect to techniques and methodology, most developing countries have less choice in alternative techniques that can be used by industrialized countries, but have a wider range of alternatives than centrally-planned economies. This is largely because of the existence of a private sector of varying degrees of strength and capability in most developing countries.

It is against this background, that a different approach towards privatization needs to be adopted in most developing countries and that several key issues in this regard need to be carefully assessed. These include the specific objectives sought to be achieved through privatization; the changing context of increased market orientation and private-sector development in industrial subsectors and related infrastructure and service enterprises; the preparatory or pre-privatization measures to be undertaken prior to invitation of offers, including restructuring of the enterprise and determination and valuation of assets to be privatized; assessment of the implications of privatization, including local or foreign ownership of privatized assets; the selection of enterprises to be privatized; the availability and mobilization of local private-sector investments, and the need and potential for foreign investment and participation.

B. OBJECTIVES: IN PURSUIT OF EFFICIENCY

The objectives of privatization in developing countries can range from those which are directly related to the state-owned enterprise in question and to broader goals of governmental economic policy.[1/] The former include financial savings otherwise payable as subsidies or debt repayments to meet the losses of most such enterprises; income and earnings from sale of such enterprises, and greater efficiency and competitive capability of such enterprises, which often occupy a pivotal role in their respective sectors of production and services. Only the last-named consideration would be applicable in the case of SOEs which are making profits and yielding reasonable returns, usually in sectors such as transportation or telecommunications but also in mining and manufacturing. In such cases, an important objective may also be to ensure inflow of new investments and modern technology and management expertise through private-sector participation. The broader policy objectives can extend from overall debt relief, which constituted an important basis for privatization in several Latin American and some Asian and African countries in the 1980s, to the major shift in national policies to market-oriented economies. The latter objective was the principal reason for privatization in former centrally-planned economies, where privatization extended to most fields and sectors, as also in several developing countries where it has been largely concentrated in certain infrastructure, service and production enterprises. The distribution of ownership of such enterprises to the private sector was also of importance in several countries, both industrialized and developing, where privatization was employed to encourage and promote ownership of, and investments in, state-owned enterprises by the private sector. The motivation for privatization of particular enterprises has often been a mix of various factors and conditions and has to be assessed on a case-by-case basis, as the mechanism utilized for privatization may largely depend on the goals sought to be achieved.

As against the principal objective of reducing the financial burden of inefficient SOEs in most African countries, multiple objectives have generally been sought to be achieved in most Latin American and Asian countries, ranging from securing debt relief and improving efficiency and competitiveness of SOEs in several Latin American countries, to ensuring greater competitive efficiency and improved technology usage in most Asian countries, besides reduction of financial liabilities of such enterprises. It is expected, in these countries, that transfer of public ownership to private investors will substantially improve the efficiency, productivity and competitive capability of privatized industrial enterprises; generate revenues from the sale of such companies and assets for the government, and reduce budget deficits resulting from continuing subsidies and financing of such companies.[2/] Privatization also aims to strengthen the private sector, both through it increased participation in industrial development and exports and in strengthening of the capital market. In several sectors, ranging from infrastructure such as telecommunications and air transportation to financial and other services and in various manufacturing subsectors, transfer of ownership from the public sector to private investors has also been motivated by the increasing financial resources required for modernization and expansion in these fields, together with acquisition and application of modern technological and managerial expertise. A decade of debt burden and scarce financial resources also resulted in considerable under-capitalization in several developing countries of infrastructure investments, particularly in telecommunications and transportation, where major technological developments have taken place. The requirement for major capital infusion has also become important in manufacturing subsectors, where new and competitive technologies have to be utilized.

The modernization of basic and technological infrastructure facilities such as telecommunication networks, transportation, international airlines, highway and railway systems and port facilities are essential prerequisites for further productive industrial investments by domestic and foreign investors. In countries with significant natural resources, expansion and exploitation of minerals, has also increasingly been constrained by under-capitalization of such activities. In industrial subsectors, where such activities have traditionally been reserved for the SOEs, varying degrees of partial privatization have increasingly taken place, largely through local private investors. The need to mobilize additional financial resources and apply new technologies and management expertise as part of modernization has also induced several countries to transfer public ownership to the private sector in the iron and steel, petrochemical and engineering industries. Several governments have also undertaken privatization of sugar mills, textile plants, and other industrial and manufacturing activities where the bureaucratic decision-making process of SOEs made such enterprises unresponsive to rapidly changing demand structures and higher standards of performance.

With the large proportion of production and service activities run by SOEs, and the key role of such enterprises in infrastructure and basic industries and in various industrial subsectors and industry-related services in several developing countries in Latin America, Africa and Asia, the privatization process has become an important socio-economic and political issue. The objectives of privatization and the method of implementation have been determined as much by the socio-political considerations as by economic factors and these considerations have had considerable impact on planned privatization. They have also strongly influenced decisions relating to the acceptable method of privatization.

C. MARKET ORIENTATION AND PRIVATE-SECTOR DEVELOPMENT: KEY ISSUES

The increased emphasis in most developing countries on market-oriented industrial growth, and on the enhanced role of the private sector in industry, has been a critical factor in determining the scope and nature of privatization in various developing countries. In several Asian countries such as the newly-industrializing countries of the Republic of Korea, Singapore and Taiwan Province of China and the rapidly-expanding economies of Indonesia, Malaysia and Thailand, as well as in a number of Latin American countries, particularly Brazil, Chile, Mexico and Argentina, private-sector industry has constituted the principal engine of growth in recent decades. Even greater emphasis is now being placed on the private sector's role in industry in these countries, as also in most developing countries of Africa, Asia and Latin America and the Caribbean. Privatization must be viewed as an essential element of private-sector development and policies relating to privatization must be considered within the broader framework of industrialization through the private sector.

Transfer of ownership

The issue of ownership of privatized enterprises has often constituted an important factor, in several developing countries. In centrally-planned economies, such as China and Viet Nam, the establishment of joint ventures by state-owned enterprises with foreign companies can involve transfer of ownership of existing industrial assets and implies partial privatization. In developing market economies, transfer of ownership to foreign enterprises through privatization may, however, be restricted as a condition of the offer. In Brazil, the Privatization Law limits foreign ownership to 49 per cent while, in Mexico, until recent modification of the 1973 legislation regulating foreign investments, foreign ownership in most sectors was limited to a minority position. In India, restrictions on privatization through foreign investments continue, despite extensive recent liberalization. Foreign ownership in the banking sector still continues to be restricted in a number of developing countries. Restrictions on transfer of ownership may not necessarily be confined to transfer to foreign transnational corporations (TNCs). In Malaysia, for example, the Guidelines on Privatization specify that the ownership structure should be at least 30 per cent Bumiputra, (local Malaysian), and a maximum of 30 per cent foreign. In several developing countries, there continues to be concern regarding a high degree of concentration of economic wealth and power among a few industrial groups.

Selection of enterprises to be privatized

An important issue is the determination of criteria for selection of enterprises to be privatized. These may be directly related to the overall objectives of privatization, as discussed above, or to specific needs and priorities in particular subsectors. A critical aspect for consideration may be whether profitable state-owned industrial enterprises should be privatized, and whether privatization should be extended to enterprises being operated as public monopolies, both at a profit and meeting essential needs, such as electricity generation or distribution, and telecommunications, apart from service enterprises such as airlines and hotels.

Availability of local private-sector capital

An important constraint in several developing countries is the inadequate availability of local private-sector capital to purchase the shares of privatized state enterprises, particularly if an extensive privatization programme is undertaken during a short period. This is particularly applicable in African developing countries, where local capital markets are inadequately developed. In the case of several Latin American and Asian countries, private-sector capital has, in most cases, been forthcoming to a substantial extent, and both public offerings and private placements may be possible, provided the privatization offer is considered attractive in terms of profitability and returns and provided the requirements of local capital for the overall privatization programme are not too high and are spaced over a period of time.

Foreign capital participation

A major issue for consideration is whether privatization should aim at obtaining varying degrees of foreign participation, ranging from outright foreign acquisition of the SOEs to varying levels of foreign ownership. Foreign participation can take the form of outright purchase as has taken place in Poland, Hungary and other east European countries. It can also be limited to different levels of participation in combination with banks and local private-sector business groups. The implications of different levels of foreign participation need to be assessed. A considerable element of flexibility may, however, be necessary, once the decision to privatize is taken.

Enterprise restructuring

One of the critical issues in privatization is the extent of enterprise restructuring that needs to be undertaken prior to privatization. It has initially to be determined whether any such restructuring is necessary at all, and whether, once a decision to privatize is taken, the matter is left solely to market forces. This has been the approach in several formerly centrally-planned economies, as also in the case of privatization of several large corporations in industrialized countries. The argument in such cases is that the enterprise, or shareholding pertaining to an enterprise, should be sold or transferred on an "as is" basis, with the price or conditions of transfer being dictated by market conditions. It is further argued in such cases that any restructuring exercise may well lead to considerable fruitless expenditure if this is not fully reflected in the increased value of the