ISSN 0351-3564

INTERNATIONAL CENTER FOR
PROMOTION OF ENTERPRISES

PUBLIC ENTERPRISE

Quarterly Journal

Vol. 18, Nos. 1-4

THEMATIC EDITION

MODELS OF THE STATE OWNERSHIP FUNCTION ORGANIZATION

Proceedings of the High Level Meeting of the State Ownership Authorities, 5-6 September 2011, Ljubljana, Slovenia

An Experience through Disinvestment in India

Advancing Human Rights at the Corporate Level: New Challenges and Opportunities

Edited by Štefan Bogdan Šalej

PUBLIC ENTERPRISE, 2011, Vol. 18, PP. 1-114, Ljubljana, January-December 2011

International Center for Promotion of Enterprises
ICPE

PUBLIC ENTERPRISE

Quarterly Journal vol. 18, Nos. 1-4

MODELS OF THE STATE OWNERSHIP FUNCTION ORGANIZATION

Proceedings of the High Level Meeting of the State Ownership Authorities, 5-6 September 2011, Ljubljana, Slovenia

An Experience through Disinvestment in India

Advancing Human Rights at the Corporate Level: New Challenges and Opportunities

Edited by Štefan Bogdan Šalej

EDITOR:
Štefan Bogdan Šalej

ASSISTANT EDITOR:
Suzana Saptefrati

Published by the International Center for Promotion of Enterprises
Dunajska 104, 1001 Ljubljana, Slovenia, EU
Tel: +386 1 568 2331; Fax: +386 1 568 2775

Print: Grafika Gracer

Print run: 500

CONTENTS

FOREWORD

by Dr. Štefan Bogdan Šalej[1]

Dear Readers,

The papers contained in this publication are based on the selected presentations from the notable event High Level Meeting of the State Ownership Authorities "State as an owner – ownership policy, execution of state interests and fostering of public-private dialogue", organized by the ICPE, as the integral part of our efforts to place public attention on the current issues of public enterprises in the new economic and social framework.

Despite the waves of privatization in the eighties and nineties, public enterprises remain important producers of goods and services worldwide and recently even became one of the key drivers of emerging-market economies' growth. Public sector enterprises exist in all countries independently of their development stage. They are part of government development policies, and the success of overall economic policies, especially in developing countries, sometimes depends on their efficiency and contribution to the national economy. Badly managed public sector companies are not bad only for their governments; they are an erosive factor in social relationships, as they increase the poverty level.

So efficient management is crucial; the fundamental step in this is creating efficient, transparent and independent top management. It does not matter very much if the country decides to have an agency, government or ministry department, as this is only the formal part of government organization. What is crucial are clear objectives and rational visions for public enterprises established by political institutions like parliament and government. It is not possible to achieve good performance if you do not know what you want or if private political interests prevail over the national interest.

Our studies in selected countries are clearly pointing to such conclusions, and the responsibility to manage public sector enterprises is much greater, since we are talking about leading development and economic policy partners. If public enterprises fail, it strongly affects the country's economy, its public finances and especially the private sector. The economic and even political consequences are disastrous.

[1] Director General, International Center for Promotion of Enterprises

Numerous examples of public sector enterprises (PSEs) in previous years successfully operating in competitive global markets clearly illustrate that public sector enterprises can match the performance of their private-owned counterparts if they are properly governed. However, in many countries PSEs still suffer from inappropriate governance, which results in a loss-making, non-transparent and inefficient PSE sector.

Hence, there is general agreement between the policymakers and all other stakeholders to implement reforms to create the environment for market and profit oriented PSEs. During the last decade, the reform of PSEs toward improving their performances was the subject of wide discussions, as they face specific governance issues that make them more difficult to reform than private sector enterprises such as managers', politicians' or bureaucrats' self-interested behaviour, the non-market mechanism and a low level of disclosure.

Unlike private enterprises whose primary objective is the maximization of profit and economic value added, PSEs might pursue both commercial and non-commercial and thus possibly conflicting objectives if governing entities have different aims for one public enterprise. This issue could be addressed to the organization of the state ownership function, or in other words to the separation between management and ownership, which remains one of the key questions regarding the debate on efficient PSE performance. The ownership function of the state could be generally exercised in centralized, decentralized or dual manners (World Bank 2006). In the centralized form, one governmental authority, such as a ministry or holding company, would be responsible for the government's shareholdings in all PSEs. In the decentralized model, different enterprises would be overseen by different ministries, and PSEs might also have widely varying requirements and relationships with other parts of the administration. In the dual form, one single governmental entity would perform certain ownership functions for all PSEs (varying from being close to that of the centralized case to only very limited control over PSEs), but other functions would be performed by different entities for different SOEs.

The model of decentralized or dual ownership has often been criticized due to the dual role of the overseeing ministries in determining the industrial policy and evaluating performance of PSE, so the centralization of ownership function has been strongly advocated in recent years. However, diversity in management and ownership models among countries worldwide remains: as each country has developed its own model of exercising ownership, it has continued searching for the role model of effective state owned ownership, which will assure both achievements of commercial and policy objectives.

One of the most significant results in the process of the restructuring of the PSEs environment was the issuing of the Guidelines for the Corporate Governance of the State-Owned Enterprises by the Organization for Economic Co-operation and Development (OECD) which among other issues also recommend centralization of the ownership function. Guidelines have been very well received and recognized not only by OECD Member States but also by other countries regarding the quite high corporate governance standards; however, specific historical, social and political contexts of national economic environments present difficulties in their implementation.

In order to contribute to further discussions on reforms for the public sector, ICPE initiated the High Level Meeting of the State Ownership Authorities. As recent experiences with EU debt crises show that the policy of "one-size-fits-all" might not be the best solution regarding different political and economic environments even in countries with similar economic and political systems, we also believed that beyond some clearly needed general recommendations on PSE governance, successful implementation of reforms requires taking into consideration specific conditions within each country.

Apart from the standard debates on the organization of the ownership function, ICPE also recognized that in many countries due to the complex political situation, political commitment to the implementation of the reforms could be a key factor in its success.

The ICPE – International Center for Promotion of Enterprises – an intergovernmental organization founded 35 years ago, was proud to host the representatives of ownership agencies and institutions of state holdings to discuss the abovementioned issues and challenges of public enterprises. The Meeting held in Ljubljana was a great success: in the four panel sessions 28 speakers presented the organization of the state ownership function for 26 different countries (Albania, Angola, Bangladesh, Belarus, Bosnia and Herzegovina, Botswana, Brazil, Bulgaria, Colombia, Egypt, Georgia, Germany, Hungary, Latvia, Lithuania, Malaysia, The Netherlands, Panama, Peru, The Philippines, Slovakia, Slovenia, South Africa, Turkey, The United Kingdom and Zambia). In addition to this, one corporate case from Slovenia was presented by Mr. Ales Hauc, General Manager of the Slovenian postal service.

During the panel sessions, a wide range of PSE governance models were discussed. Basically, in regard to some general considerations of PSE governance issues, countries can be roughly classified into three groups. The first group contains countries that have concluded the privatization process and kept their ownership share just in enterprises which are used as a tool to fulfill specific and significant tasks that cannot be achieved better or more economically in any other way. The second group of countries recognized the necessity of significant involvement of the government in the economy. Based on that, these countries kept a large share of the economy under the government of the state, mostly with the objective of obtaining social justice and higher levels of employment. Finally, some countries expressed their strategic goal to begin and continue the privatization process to a larger extent, and they have been looking for positive experiences from the countries that have already come through the major waves of privatizing state holdings.

However, despite the significant differences in views on the role and governance models, participants generally agreed that the crucial precondition for successful governance of the PSEs is the clear setting of the objectives, which government wants to achieve through the PSEs. Clearly defined objectives, together with the introduction of Corporate Governance principles, could make PSEs a powerful tool for achieving different goals of economic policy, and at the same time, become competitive players in the market game with private sector enterprises.

This publication brings forth the papers based on selected presentations from the Meeting. We have tried to make this selection based on the principle of diversity, thus to include presentations of the countries from the different continents, with different levels of economic development, different models of organization of the state ownership function and different philosophies toward the role of PSEs in the national economy. We also tried to organize the presentation similar to the three-part papers, wherever it was possible, with the structure: the historical background, the current state of PSEs and concluding remarks and future prospects of PSEs. We would like to stress that in this publication, the phrase Public Sector Enterprise (PSEs) is used as the general term for the enterprises in state ownership, independently from the country specific equivalent phrase (State-owned enterprises, Government linked companies, etc.). We have included in the present volume of the Public Enterprise Quarterly Journal only the contributions we have received as at the closing date of the current issue, while the rest of the articles will be published in the next edition of the PE Journal.

In addition to the articles based on the High Level Meeting of the State Ownership Authorities speakers' contributions two other excellent papers are presented. The first deals with the issue of disinvestment in India, and, more precisely, it aims to assess the financial performance of the disinvested central public sector enterprises (PSEs), mainly in so far as profitability and operating efficiency are concerned. The second tackles the very sensitive topic of human rights at the corporate level and represents a review of the United Nations' guidelines on business and human rights while offering some insights on the way in which the newly-established Working Group on human rights, transnational corporations and other business enterprises appointed by the UN Human Rights Council can assist the corporate sector in implementing the guidelines.

I would like to thank to all distinguished speakers for their valuable contributions to the success of our Meeting and this publication. I would also like to acknowledge and to express my deep gratitude to the Ministry of Finance for its high patronage of the High Level Meeting[2].

[2] In certain parts of the present issue of the Public Enterprise Quarterly journal, especially those referring to the High Level Meeting of the State Ownership Authorities, we benefited from the assistance of Aleksandar Zdravković and Draško Nikolić.

State as an owner – ownership policy, execution of state interests and fostering public-private dialogue: The Albanian Case

Majlind Lazimi[3]

1. Historical Background

Since the period of communism, when nearly everything was state owned, Albania has gone through the dramatic process of transition reforms. The radical political and economic transformation in early 1990s included the following reforms:

- Change of regime from the planned economy to free market economy policies; "Shock therapy" was fully implemented with the liberalisation of prices, etc.

- Restructuring of the public sector – phasing-out subsidies for public enterprises and fostering free market entrepreneurship

- Privatisation of the economy – mixed privatisation through transfers of ownership from public to private hands aiming at upgrading living standards and ensuring social justice by abandoning the inefficiency and low productivity of state ownership

Whereas privatisation has been widely considered as a "restructuring process" in the western world, in Albania, as in many post-communist countries, privatisation has been perceived as a "systemic transformation" of the whole society.

The process of privatisation in Albania was implemented in two phases:

- 1991–1999: privatisation of SMEs took place, e.g. direct sale, public auction and liquidation

- 1999 onwards: privatisation of "strategic sectors" has been on the agenda of all governments. Strategic sectors in this context include Telecommunications, Energy, Infrastructure & Transportation, Banking, the mineral industry, oil and gas, etc.

[3] Chief of Staff, Ministry of Economy, Trade and Energy

The main "drivers" behind all this privatisation were to raise new capital and heal the financial problems of the state owned enterprises to improve production levels and service quality along with price reductions for the consumers, and to apply new technologies and know-how – all these under the premise of better management.

Privatisation strategy has aimed mainly the following objectives:

- Revitalisation of the economy through efficient exploitation of human and natural resources, e.g. job creation and increases in income
- Ensuring economic growth and sustainable development, e.g. reducing public debt and budget deficits
- Supporting and enhancing the private sector in the production of goods and services (currently the private sector comprises 85% of the economy) – increasing both competition in the market and the quality of goods and services
- Attracting strategic investors in priority sectors (both domestic and foreign)
- Improving the business climate and boosting the creation of capital markets

2. Current State of PSEs

In 1995 by means of a Parliamentary Act, all PSEs had to be transformed into state commercial companies, mostly in the form of joint stock companies, and comply with relevant provisions in force at the time, i.e. the "Law on Commercial Companies" (1992).

The Ministry of Economy (now Ministry of Economy, Trade and Energy – METE) was legally designed to be the exclusive legal representative of the State's ownership and the only state authority responsible for the implementation of the strategy for transforming state enterprises into joint-stock companies, e.g. METE appoints supervisory boards, confirms financial statements and approves business and investment plans.

On the other hand, Albania has adopted a "decentralised model" where other ministries, various state departments and institutions and local authorities are responsible for the management of all property and state companies that fall under their legal functions.

Thus, from a legal point of view, each ministry is responsible for determining the strategic goals of the state companies which they oversee. These ministries are now responsible for achieving state companies' goals through the wide participation of their representatives in the boards of directors by drafting, approving and enforcing the state companies' objectives.

With the new law on commercial companies which entered into force at the end of 2008, state companies are qualified as companies in the public offer. This has enhanced the legal mechanism for exercising state control related to management aspects (privatisation of OSSH).

3. Concluding Remarks and Future Prospects of PSEs

The Albanian economy during communism followed a policy of self-sufficiency, much like modern-day North Korea, which resulted in the inability of state entities to serve the needs of the new economic system due to the following issues:

- Old technology and lack of investments
- High cost and high debt of public enterprises
- Blocked market and large debts
- Lack of adequate management and impossibility of bankruptcy
- Unclear financial objectives
- Strong political influence damaging the economic activity of PSEs
- Lack of practices of corporate governance

The difficult situation in all sectors of the economy in the early 90s required structural reforms, liberalisation and deregulation policies associated with privatisation. Mainly, the above reasons and competitive imported products forced most PSEs to fail.

The following process of privatisation in Albania has encompassed transferring 3 main rights from the state to the private sector:

- Ownership rights – the state is relinquished from all the risks associated with the management of enterprises
- Exploitation rights and development rights – the state reserves the right to monitor concession agreements with or without the financial risks involved

As major privatisations in key sectors of the economy have taken place, Public-Private Partnership Schemes are gaining momentum. Within this framework, the government and private sector have new roles:

- New role of the government: establishing great reforms aimed at improvement of the business climate, e.g. flat tax regime, one-stop-shop, e-public procurement, etc.

- New role of the private sector – active contribution in public investments and services, e.g. concessions in energy (hydro), transportation (TIA), oil-gas (Bankers Petroleum), etc.

Regarding the implementation of the principles of Corporate Governance, Albania basically follows the Continental European model , e.g. auditing, board and management structures, corporate responsibility and compliance, financial transparency and information disclosure, ownership structure, exercise of control rights, etc. While the majority of these principles have been implemented in Albania, it still lags in the development of its capital market.

Bangladesh: Transforming Public Enterprises

A. B. M. Khorshed Alam[4]

1. Current State of PSEs

Regarding the level of ownership, Public Sector Enterprises in Bangladesh can be divided into three categories:

- 100% Government-owned companies
- Companies with up to 49% offloaded shares and managed by public sector
- Companies with more than 51% offloaded shares and managed by private sector:
    - National companies
    - Foreign companies including multinationals

Some basic facts on PSEs in Bangladesh are presented in Table 1.

Table 1 – PSEs in Bangladesh at a glance

No. of PSEs	236 units
PSEs contribution to GDP	2%
No. of PSEs listed on Stock Market	27 units
Market capitalisation of PSEs	10.30%
Total Market Capitalisation	US $49.86 bn
PSEs' Employment out of total employment	7%
Total Employment of PSEs	240,000
PSEs Privatised through outright sale	54
No. of PSEs to be listed on Stock Market	5

Public Sector Enterprises are operating in the majority of sectors in the national economy: financial (commercial banks & financial institutions), manufacturing (jute industries, textile industries, engineering industries, chemical industries, sugar &

[4] Additional Secretary, Ministry of Industries

food industries, forest industries, power, gas, water, medicine, etc.), transport and communication (road transport, water transport and aviation), trade (energy and commodities), agriculture (fertilizer distribution, fisheries), construction (urban development and the housing authority) and service sectors (SME development, tourism, regulatory bodies, etc.).

PSEs operate in Bangladesh for various reasons, and the state or purpose of PSE functioning can be summarised as follows:

- Historically inherited large industrial entities
- Monitor and guide the financial sector by means of commercial banks and financial institutions
- Huge capital intensive, nationally important projects like power plants, fertilizer factories, etc.
- Commercial entities required to protect public interest, e.g. sugar mills, commodity distribution companies, etc.
- Ensure basic necessities for the citizens, like water supply, sanitation, urban transportation, etc.

In regard to centralisation at the level of the ownership function, no central ownership authority exists in Bangladesh. As many as 19 ministries own the PSEs in Bangladesh. The Organization of the State Ownership Function for PSEs could be illustrated by the scheme:

Cabinet of Ministers => Respective Ministry => Corporation Board => Enterprise Board => Enterprise Management

Different governmental bodies perform different tasks in the process of PSE governance. Performance is monitored by the Holding Corporation while the budget is controlled by the Ministry of Finance. Appointment of the CEO and Directors of the Holding Corporation is controlled by the Ministry of Human Resources. Appointment of the CEO and top management of enterprises is controlled by the Holding Corporation or the Enterprise Board. Pay structure of PSE workers is determined by the Wage Commission under the Ministry of Labour and Employment. Company Law is controlled by the Ministry of Commerce. Capital expenditures for expansion, modernisation, renovation, etc. through government financing is controlled by the Ministry of Planning. The overall administration of PSEs and Holding Corporations is vested with the respective Ministry.

Performance Evaluation Systems of PSEs are executed through the different entities: target setting and performance evaluation is performed by the Enterprise Board, internal auditing by the Holding Corporation, auditing by the government commercial audit department under the Comptroller and Auditor General of Bangladesh and external auditing by a qualified chartered accounting firm. Capital expenditures, if funded by government, are monitored and evaluated by the Implementation, Monitoring and Evaluation Division of the Ministry of Planning.

Regarding the practices in the nomination of directors of the PSE Board in Bangladesh, there are no specific rules or policy guidelines. Administrative ministries appoint the bureaucrats, professionals, business leaders and members of civil society. Political consideration is a usual practice. The Company Act, SEC guidelines and Bangladesh Bank's regulation generally provide a framework without any specific instruction to the government nominated directors. Statutes spell out the powers of the board but are sometimes influenced by the respective Ministry. Boards are composed of 7–13 members on average. Selection of a CEO and top managers is executed through appointments from civil service on deputation, on contract or via political affiliation.

Concerning the remuneration policy, with few exceptions, the majority of the board of directors follows government pay scales. Non-executive directors only get a fee for attending the board meeting. Performance of the boards is not evaluated.

3. Concluding Remarks and Future Prospects of PSEs

A policy shift on PSEs is based on several considerations. Employment must be considered before privatizing any public sector enterprise. Alternative employment of the existing workforce has to be ensured. PSEs will be encouraged to function to supplement and as a competitor to the private sector. In this regard, establishing public private partnerships (PPPs) and running industries through private management will be given priority. Local and international entrepreneurs will be invited to invest in the PSEs for their technological and managerial development. If privatisation could bring benefits to officials, employees and workers, it will be given priority.

Key elements of the Reform Strategies of Public Sector Enterprises:

- The private sector shall be the key role player in the development of industrialisation.
- Government will examine the probable ways to make PSEs profitable before pursuing privatisation attempts to be taken towards managerial development in public enterprises and shares to be offloaded to clear the way for creating a

Public Ltd. Co. under the Company Act, 1994.

- Government will conduct a survey on technical and financial aspects of privatised enterprises to take account of their visible & invisible impacts on the national economy, and do what is necessary to address any problems.
- Priority shall be given to encourage establishing enterprises under Public Private Partnership (PPP) and to running industries via the private sector.
- Infrastructure projects like CETP, electricity, gas, port facilities, road and railway transportation, telecommunications, etc. in economic zones and industrial parks will get priority under PPP initiatives.

In addition, key measures of the PSE Board reforms are listed:

- Re-constitution of the PSE Board including State-owned Commercial Banks (SCBs)
- Provision made for independent directors on boards of listed companies
- Corporatisation of the SCBs
- Term limits on board duration and limits to the size of the boards
- Implementation of BASEL II Framework from January 2010
- Separate Banking Division under the Ministry of Finance
- Separate pay scale for the SCBs and Bangladesh Bank (BB) (proposed)
- Banking Reform Law (proposed)
- Financial Reporting Council 2008 (in process)

Belarus: Public Sector Development

Dmitry Kolkin[5]

1. Historical Background

Belarus started its development as a country with a socially-oriented market economy upon its independence in 1991. A significant portion of the state budget is spent on social needs.

Belarus achieved an average 7.5 percent annual GDP growth in the ten years up to 2008, benefiting from its inherent strengths and favorable external conditions. High investment-to-GDP ratios and productivity gains from a well-educated and disciplined labor force were the main contributors to growth.

Belarus is a country with huge industrial capacity and several competitive advantages (such as a valuable geographic position, educated and inexpensive workforce, well-developed research centers and an existing industrial structure). Its GDP and industry structure have not changed significantly since 1992, and the key drivers of Belarus' economy are state-owned companies mainly from industry, trade and construction.

Since Belarus gained its independence in 1991, the state sector has not changed significantly in terms of its fixed assets structure and employment structure: the primary parts of these indicators belong to the public sector.

2. Current state of PSE sector

In general, the public sector remains a key driver of economic performance in Belarus:

- 70% of enterprises have a state share in authorized funds
- almost 60% of fixed assets belong to the state
- One in two employees is employed by public enterprises

Comparisons between the Russian Federation, Kazakhstan and Belarus in terms of fixed asset structure and employment in regard to ownership structure are given in Figure 1 and Figure 2, respectively.

[5] Advisor to the Minister, Ministry of Economy

Figure 1 – Fixed Asset Structure by Ownership

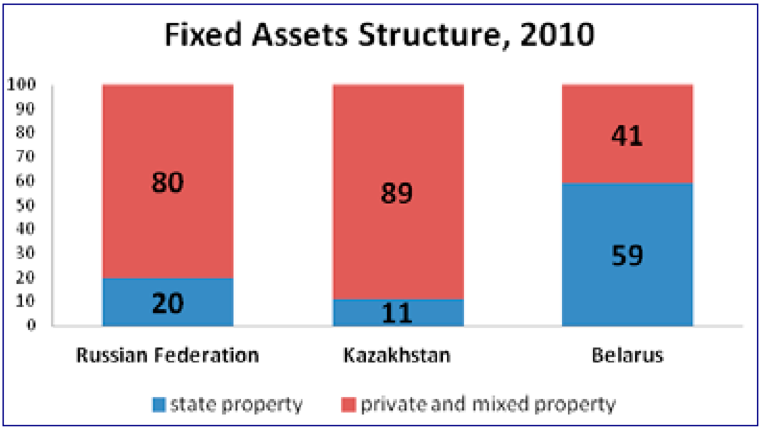
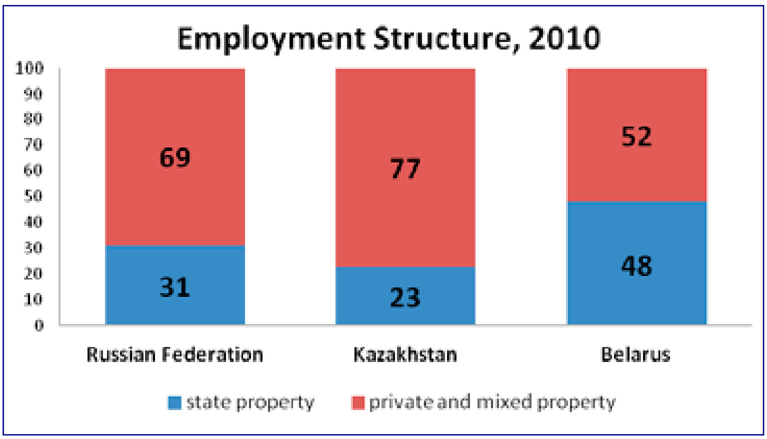


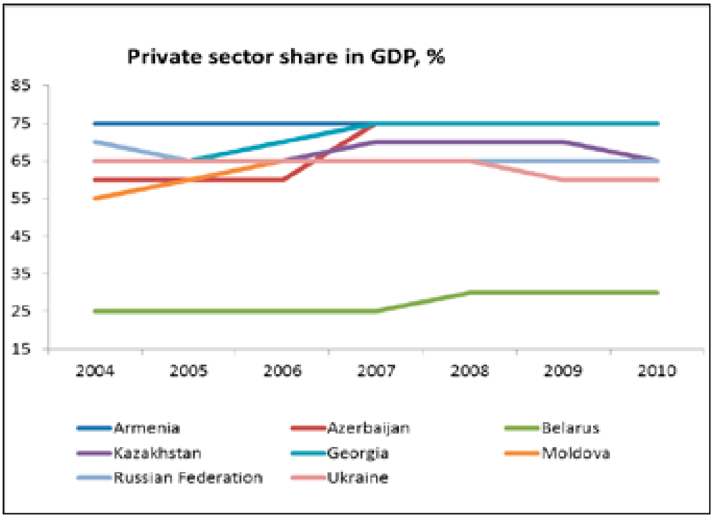
Figure 2 – Employment Structure by Ownership



Although FDI inflow is growing from year to year, investment primarily is going to "greenfield" projects. This process does not significantly contribute to changing the economy's structure in terms of creating a strong private sector, which could be a key driver of future economic performance.

The size of the state sector is the largest among CIS countries (Figure 3) and Eastern Partnership countries, and it accounts for almost 70% of GDP.

Figure 3 – Share of the Private Sector in CIS Countries



3. Concluding remarks and future prospects of the PSEs sector

Since 2007, it was decided that the private sector should participate more broadly in supporting sustainable economic growth. Several government incentives were introduced in terms of enhancing private sector development: mainly in taxation, registration and licensing.

Although Belarus has moved to 68th place in the Doing Business Report 2011, it still remains a country with a high level of bureaucracy that needs to be reduced for future private sector growth.

Until 2008, Belarus did not use a mechanism of economic restructuring such as privatization for several reasons; most important of them is that the majority of enterprises remaining from the USSR period was in good condition and could produce competitive products, mainly for its own local and other CIS countries' markets.

Although there were a couple of privatization deals during this period, privatization did not achieve a high level of development.

Having used the potential remaining from the USSR era, it was decided to switch from only supporting the development of large state-owned companies to selling them off to strategic investors. And in 2008, a new mechanism of privatization was introduced: the creation of 3-year plans that helped to create a transparent and consistent framework.

At this point there are two such plans: one was for the period of 2008-2011, and the other one is for 2011-2013. The results of the 1st plan's realization were not successful: only 16% of enterprises included in the plan were sold to strategic investors. The reason for such poor results is that the conditions of privatization deals were not attractive to investors (mainly due to existing debts and special government conditions not to dismiss staff in order not to create social problems).

It was decided to review the main legislation in this process, and in 2010 new legislation for privatization was prepared in close partnership with The World Bank and International Finance Corporation. At the beginning of 2011 this law came into force.

Moreover, it was decided to create a special agency that would be in charge of implementing the new privatization mechanism along with the existing one. Such an agency was created in the spring of 2011 and comprises both investment promotion functions and privatization. Belarus will implement a project with The World Bank in which they will choose 10 state enterprises and make pilot privatization projects of them in order to see if the new privatization mechanism is more efficient than the existing one.

Since 2008, Belarus has been taking consistent steps in price liberalization: price and trade restrictions on many goods were removed. Since the beginning of 2011, the government has regulated prices on only 27 products, which are socially important for the majority of the population.

Although major economic indicators remained at optimistic levels, the Ministry of Economy forecasts a temporary slowdown in economic development in 2012 during the forthcoming transformation period connected with the restructuring of state-owned enterprises. The average GDP growth rate is expected to be 3.1% and the average unemployment rate 1.7%.

In terms of FDI Belarus is becoming a more and more attractive place to do business. In addition, the creation of the Customs Union with Russia and Kazakhstan has opened an opportunity to deliver its production to a market of 170 million people.

- Belarus has achieved high economic growth over the past 15 years
- The economic model of the country in managing its state-owned enterprises needs to be restructured for better performance
- With the help of privatization and FDI attraction, restructuring should run more efficiently
- PPP is one of the main factors in increasing corporate management in public enterprises

- Private sector contribution to GDP should increase to a level that would allow Belarus to promote it as another economic growth driver
- Although investors still find administrative procedures too complicated, the Government is improving this situation with the help of international organizations.

Public Enterprises In Botswana: Ownership And Governance

Kgotla M. Ramaphane[6]

1. Current State of PSEs

Botswana adopted a National Privatisation Policy in 2000 aimed at improving service delivery and enhancing efficiencies in Public Sector Enterprises. The Policy is managed by the Ministry of Finance and Development Planning (MFDP), thus PEEPA was established as an autonomous agency with the mandate to implement the Policy and implement privatisation transactions. Also, PEEPA advises different ministries on the appointment of the directors of public enterprises and monitors their performance and set objectives.

The privatisation policy of Botswana involves different forms of privatisation, e.g. outright sale, partial sale, outsourcing, commercialisation and restructuring. As part of the privatisation process, some of these transactions are being realised, e.g. Botswana Telecommunications Corporation and the National Development Bank.

Botswana has adopted the decentralised PE Ownership model. Mainly:

- PEs belong to different line ministries, which are representatives of the shareholders.
- The line ministers appoint the boards of directors of the PSEs that report to them.
- Most of the PEs are established through Acts of Parliament as statutory corporations while some are established as companies through the Companies Act.
- PEs are set up as autonomous bodies with their own corporate identities; they get policy direction from the line ministries, based on the National Development Plans (NDP) and the relevant ministry's strategic plans.
- The mandates of PEs are normally spelled out in their establishing documents.
- PEs submit periodic performance reports to their line ministries. The performance reviews undertaken by PEEPA have, however, revealed that oftentimes, line ministries are not adequately involved in the strategic direction of their PEs.

[6] Chief Executive Officer, Public Enterprises Evaluation and Privatisation Agency (PEEPA)

- The governance and mandates of PEs are normally provided for in the establishing documents.

The following table gives the examples of the PSEs in regard to their relevant ministries and the sectors to which they belong, as well as their generation of revenues.

Table 1 – PSEs according to sector and the generation of revenues

Ministry	Revenue Generating PSEs	Non-Revenue Generating PSEs
Agriculture	Botswana Agricultural Marketing Board Botswana Meat Commission Botswana Vaccine Institute Banyana (PTY) Ltd	Botswana College of Agriculture National Food Technology Research Centre
Lands and Housing	Botswana Housing Corporation	
Minerals, Energy & Water Resources	Botswana Power Corporation Water Utilities Corporation	
Finance and Development Planning	Botswana Development Corporation Botswana Savings Bank National Development Bank Bank of Botswana	Botswana Privatisation Asset Holdings Botswana Institute for Development Policy Analysis Botswana Stock Exchange Botswana Unified Revenue Service Financial Intelligence Agency International Financial Services Centre Motor Vehicle Accident Fund Non-Bank Financial Institutions Regulatory Authority Public Enterprises Evaluation and Privatisation Agency Public Procurement and Asset Disposal Board Statistics Botswana

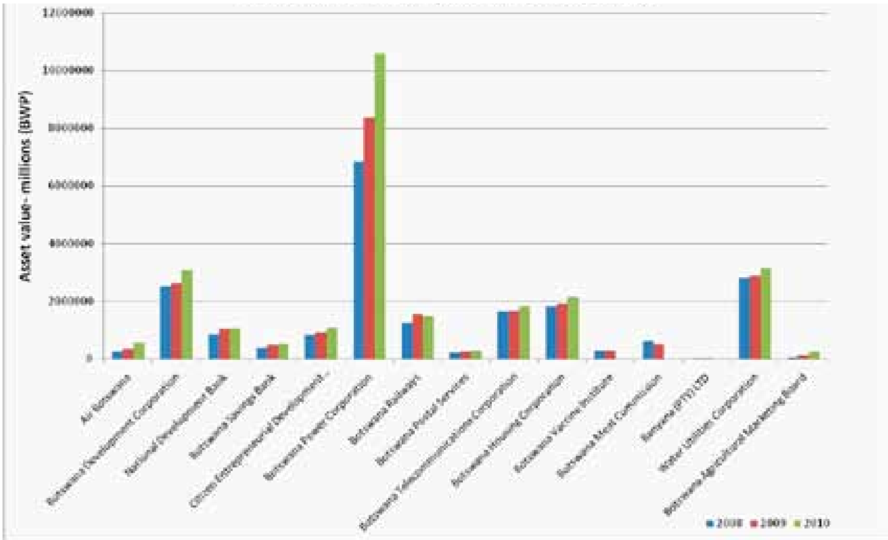
Ministry of Transport & Communications	Air Botswana Botswana Postal Services Botswana Railways Botswana Telecommunications Authority Botswana Telecoms Corporation	Civil Aviation Authority
Education and Skills Development		Botswana Examinations Council Botswana College of Distance and Open Learning Botswana International University of Science and Technology Tertiary Education Council Botswana Training Authority University of Botswana
Infrastructure, Science & Technology		Botswana Innovation Hub Botswana Technology Centre Rural Industries Promotion Company
Environment, Wildlife & Tourism		Botswana Tourism Organisation
Trade and Industry	Citizen Entrepreneurial Development Agency	Botswana Bureau of Standards Botswana Export Development & Investment Authority Competition Authority Local Enterprise Authority
State President		Botswana National Productivity Centre

Some sectors such as telecommunications have clear policies for Universal Service obligations, while the other sectors are still lagging behind with no clear policy. It is therefore common to find PSEs with dual mandates, or tasked with carrying out both commercial and non-commercial activities. PSEs are treated as arms of government and are therefore required to fulfil the developmental role of government.

As part of the broader Corporate Governance Framework, PEEPA promotes the adoption of good corporate governance practices within PSEs in Botswana which would spell out the obligations of government and PSEs, including how social obligations would be financed. Line ministries operate as owners and regulators of PSEs.

Assets value of public enterprises is presented in Figure 1.

Figure 1 – Assets value of public enterprises in Botswana



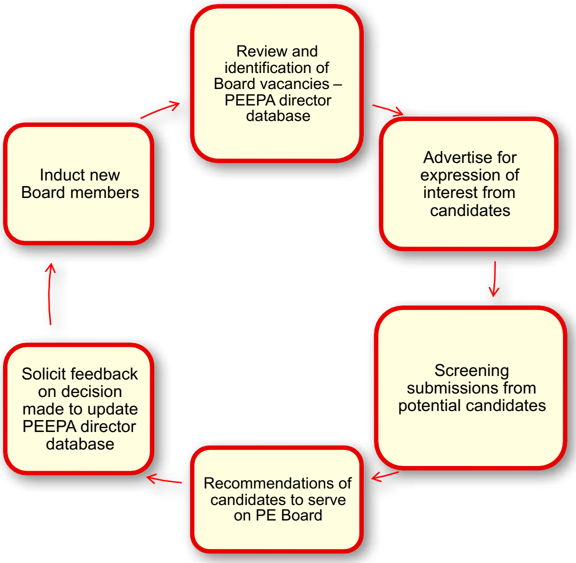
The procedure of board nomination in Botswana public enterprises can be summarised as follows:

- Board compositions are provided for in the establishing Acts/Constitutions.
- Ministers usually appoint senior Ministry officials to serve on the boards of PSEs falling under their portfolio.
- Following the approval of the Privatisation Policy of Botswana of 2000, ministries are now required to seek the assistance of PEEPA in identifying candidates to be considered for boards of PSEs.
- There is provision for candidates from the private sector to be appointed to PSE boards in order to bring private sector expertise.

- As a result there has been an increase of board members from the private sector.

Board nomination approach is illustrated in Figure 2.

Figure 2 – Board nomination process



The rationale behind the board nomination process:

- Introduce a transparent merit based director selection process
- Achieve a balanced board with respect to expertise and skills
- Identify and reduce the risk of nominating members who may be over committed
- Identify potential conflicts of interest
- Achieve continuity in the board's operation by staggering Board Membership tenure
- Promote good corporate governance

2. Concluding Remarks and Future Prospects of PSEs

Identified challenges in respect to board nomination approach include:

- Adoption of transparent merit based board nomination process not mandatory
- Restrictive provisions in some constitutive documents on the composition of the boards
- Appointment of public servants is not based on a transparent merit based approach
- Adherence to good corporate governance principles are generally not enforced
- Lack of board performance evaluation

Regarding the public enterprises performance monitoring and evaluation, the principal approach has been through annual PE Performance reviews, aimed at establishing alignment of each PE's strategy with either commercial or developmental expectations, plans and sector policies, determining the achievement of PEs' developmental objectives and resultant impact, assessing the adequacy of resourcing and internal resource utilisation, evaluating the long term financial sustainability of the PSE, evaluating the adoption of good corporate governance practices and assessing opportunities for private sector participation.

There are several opportunities for improvement, such as adoption of the Corporate Governance Framework by PEs, adoption of the Botswana Corporate Governance Code, managing commercial vs. developmental roles and the adoption of an overarching PE ownership policy.

Taking into consideration all the above mentioned issues, conclusions about further steps in the improvement of PE performance could be summarised as follows:

- Ownership model requires improvement
- Need to separate regulation from ownership
- Develop a clear PE ownership policy
- Promote private sector participation to enhance efficiency
- Continue to increase the proportion of board members from the private sector

Government Companies in Brazil

Murilo Barella[7]

1. Historical Background

After the Second World War, the State increased its role in economic activity and began to interfere in goods production and services provision through the creation and enhancement of many Public Sector Enterprises.

In the eighties and nineties, the State restricted its activities as a goods and services provider which resulted in a "wave" of privatization. The Brazilian privatization program in the nineties was a major undertaking grounded by international standards. From 1991 to July 2001, the state transferred the control of 119 firms and minority stakes in a number of companies to the private sector. Concerning the companies in which the government had a majority of controlling shares and those in which it only had minority control, the auctions produced US $67.9 billion in revenues, plus the transfer of US $18.1 billion in debt. The government also sold US $6 billion in shares of firms that remained SOEs, obtained US $10 billion from new concessions of public services to the private sector, and sold US $1.1 billion in scattered non-controlling stakes in various private companies owned by BNDES, the National Social and Economic Development Bank.

2. Current state of PSEs

Nowadays, the society has chosen to keep and maintain several enterprises under the State ownership. All PSEs in Brazil according to the activities are presented in Table 1.

Table 1 – PSEs in Brazil according to the activities

ACTIVITY	NUMBERS
Petroleum, Derivatives and Natural Gas	63
Electric Energy	19
Finance Sector	19
Services	16
Infrastructure	9
Transport	3
Research	4
Industry	4
Others	10
Total	**147**

[7] Director, Department of Coordination and Governance of State Owned Enterprises (DEST)

Considering the peculiarities of the accounting system, particularly the rules aimed at banks and similar institutions, the members of PDG budget entities are also divided into two groups:

- State productive sector – SPE: Includes the federal enterprises producing goods and services such as basic inputs, services, research, generation, transmission and distribution and transportation.
- Federal financial institutions (mostly banks): includes federal state enterprises operating in the financial market and whose activity is governed primarily by Law No. 4595 of 31 December 1964.

Data on the number of employees in both productive and financial sectors are presented in Table 2.

Table 2 – Number of employees

Productive Sector	N^0 Employees	N^0 Outscored
Brazilian Post and Telegraph Corporation (ECT)	108,392	-
PETROBRÁS Group	72,380	277,972
ELETROBRÁS Group	26,489	1,129
Brazilian Company of Airport Infrastructure (INFRAERO)	12,225	-
Federal Data Processing (SERPRO)	10,736	1,277
Brazilian Agricultural Research Corporation (EMBRAPA)	9,248	-
Others	13,918	4,753
Total	**253,388**	**285,131**

DATE: 2010-12-31

Banks	N^0 Employees	N^0 Outscored
Bank of Brazil	112,081	-
Brazilian Development Bank (BNDES)	2,675	-
Bank of Amazon	2,914	-
Bank of Northeast	5,993	-
CEF (1)	83,206	24,274
Others	1,100	-
Total	**207,969**	**24,274**

(1) Economic and financial institution

Investments in PSEs by the productive and financial sectors are presented in Table 3, while aggregate investments as the percentage of GDP are given in Figure 1.

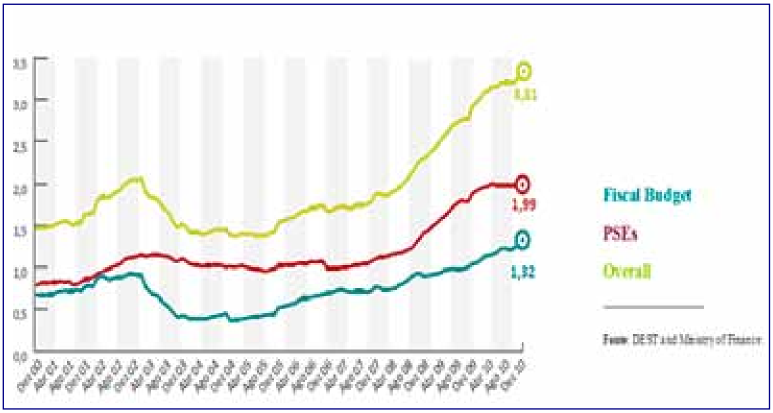
Table 3 – Investments by sectors

US $ Million

Productive Sector	2002	2009**	2010***	2011***
Eletrobrás Group	963	2,981	3,168	4,936
Petrobrás Group	3,778	35,912	44,744	543,782
Others	246	810	1,009	3,052
Banks				
Public Banks	353	1,157	1,478	2,072
Total	**5,340**	**40,860**	**50,400**	**61,791**

*Currency rates (2002-12-31) - 3,5333 Real/Brazil = 1 USD
** Currency rates (2009-12-31) - 1,7412 Real/Brazil = 1 USD
*** Currency rates (2009-12-31) - 1,6662 Real/Brazil = 1 USD

Figure 1 – Investments as the percentage of GDP



Aggregate values of assets and shareholder equity of PSEs is given in Table 4. Main financial results (net operating revenues and net income) of the PSEs' business are presented in Table 5.

Table 4 – Assets and shareholder equity

Assets	
Productive Sector	US $ Million
Petrobrás Group	312,069
Eletrobrás Group	88,165
Brazilian Agricultural Research Corporation (EMBRAPA)	540,654
Banks	
Bank of Brazil	486,840
Brazilian Development Bank	324,103
Bank of Amazon	5,078
Bank of Northeast	142,733
CEF (1)	240,436

Currency rates (2010-12-31)
1,6662 Real/Brazil = 1 USD
(1) Economic and financial institution

Shareholders′ equity (PL)	
Productive Sector	US $ Million
PETROBRÁS	186,187
ELETROBRÁS	44,330
Brazilian Agricultural Research Corporation (EMBRAPA)	477,079
Banks	
Bank of Brazil	30,273
Brazilian Development Bank	39,550
Bank of Amazon	1,161
Bank of Northeast	1,307
CEF (1)	9,813

Currency rates (2010-12-31)
1,6662 Real/Brazil = 1 USD
(1) Economic and financial institution

Table 5 – Net operating revenues and net income

Net Operating Revenues	
Productive Sector	US $ Million
PETROBRÁS	28,242
ELETROBRÁS	16,456
Banks	
Bank of Brazil	11,049
Brazilian Development Bank	8,618
Bank of Amazon	1,418
Bank of Northeast	318
CEF (1)	1,631

Currency rates (2010-12-31)
1,6662 Real/Brazil = 1 USD
(1) Economic and financial institution

Net Income	
Productive Sector	US $ Million
PETROBRÁS	21,119
ELETROBRÁS	1,349
Banks	
Bank of Brazil	7,024
Brazilian Development Bank	5,949
Bank of Amazon	85
Bank of Northeast	188
CEF (1)	2,259

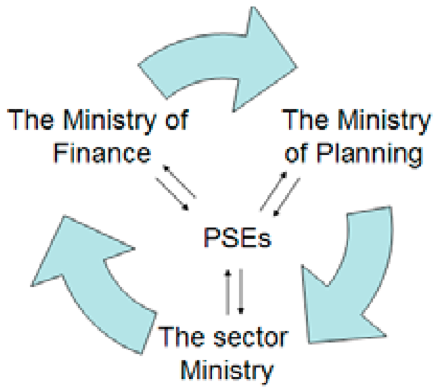
Currency rates (2010-12-31)
1,6662 Real/Brazil = 1 USD
(1) Economic and financial institution

PSEs are arranged mostly in two forms: stock and public companies. Status as a legal entity and administrative, budgetary and financial autonomy are given to PSEs in order for them to achieve their social function and fulfil their corporate purposes. This autonomy varies according to their economic dependence: the more financially independent they are the greater is their autonomy. This autonomy does not exclude the state and societal control, which is made by the National Congress through the Brazilian Court of Audit (TCU), by the Department of Coordination and Governance of State Enterprises (DEST) and by the Office of the Comptroller General (CGU).

PSEs are governed by the Brazilian Law of Corporations and, in the case of public banks, by the applicable laws of the entire financial system (Central Bank). They are ruled by the same laws governing private enterprises, including the rights and obligations in the fields of civil, commercial, labour (for contracting employees only by means of public examination) and tax laws. Public banks are also subjects of control and regulation by institutions such as the Securities and Exchange Commission of Brazil (CVM), the Brazilian Stock Exchange (BOVESPA) and the Central Bank (BACEN).

The organization of the state ownership function in Brazil is given in Figure 2. Responsibilities of each relevant institution within the execution of ownership function are presented in Box 1.

Figure 2 – State ownership function



Box 1 – Responsibilities within execution of ownership function

Ministry of Planning, Budget and Management (DEST)

- ✓ establish corporate governance guidelines
- ✓ approve the allocation of income
- ✓ approve bylaws and capital increases
- ✓ fix the board members' remuneration, and appoint one board member

Ministry of Finance

- ✓ approve the financial statements
- ✓ authorize the issuance of securities and the debt situation
- ✓ appoint one Fiscal Council member
- ✓ represent the State at the shareholders meetings

Sector Ministry

- ✓ gives orientation for the investment strategy
- ✓ sets out the board of directors
- ✓ appoints the majority of the non-executive board and Fiscal Council members

The corporate governance structure and system are presented in Figure 1 and Figure 2, respectively.

Figure 3 – PSE corporate governance structure

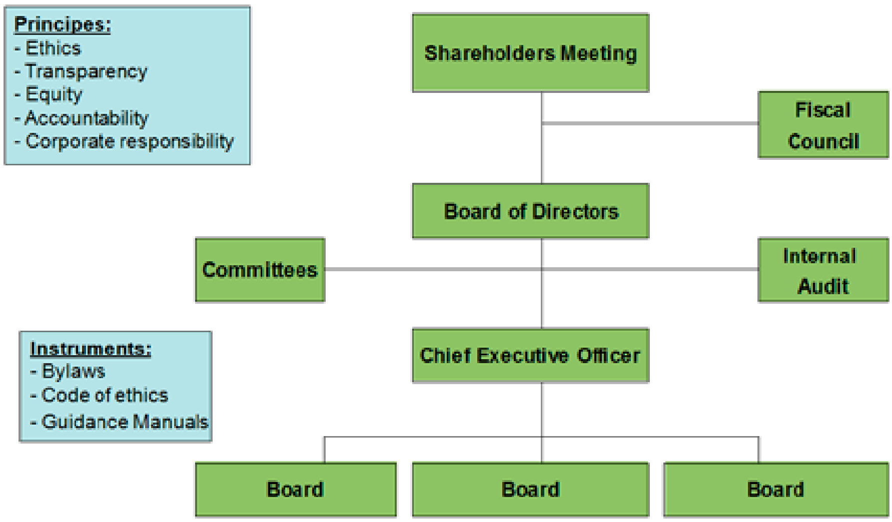
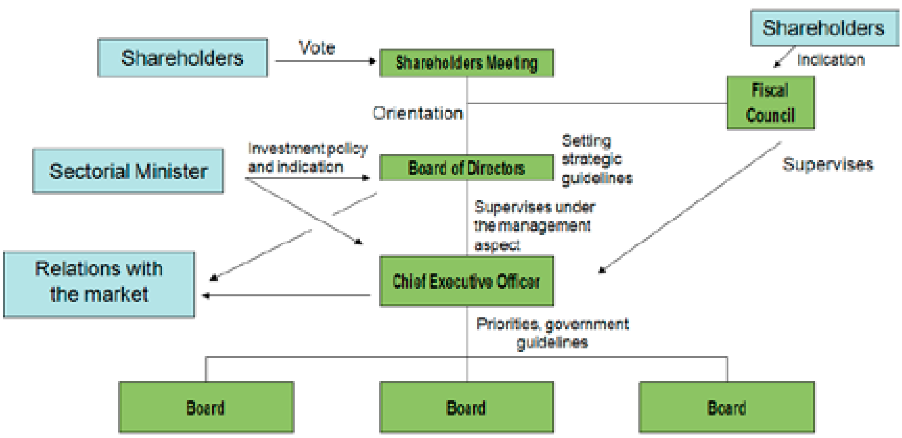


Figure 4 – Corporate governance system



3. Concluding Remarks and Future Prospects of PSEs

The Interministerial Corporate Governance and Federal Government Management of Participation Commission (CGPAR) is an authority established to decide and control the execution of the proposed guidelines for managing PSEs which acts as an executive group for technical and managerial support. Its members:

- Minister of State of Planning, Budget, and Management
- Minister of State of Finance
- Chief of the Presidential Staff Office
- Other Ministers of State (subject is under this portfolio)

Until December 2010, CGPAR's proposed set of guidelines including the following:

- Binding of the internal audit of the board of directors
- Adoption or strengthening of actions that have to give transparency to the company's activities and the use of public resources with emphasis on advertising decisions and financial flows, such as social accountability
- Emphasis on independence, impartiality and professionalism of the agents making up the frames of internal control
- The internal audit of each company will be restricted to the execution of their typical activities, preventing the diversion of functions and preserving its neutrality and impartiality
- Adoption of specific regulations for the internal auditing body
- The internal audit can be the basis of risk management advice to senior management
- The internal audit should maintain institutional relations with the organs of control (CGU, TCU, etc.)
- The segregation of function between the chairman of the board and chief executive of the company
- The practice of holding executive sessions without the presence of the chairman and directors when they are members of the board
- The approval of the annual audit plan and the annual audit report by the board without the presence of the CEO at the formal meeting of the board

- Creating support committees for decisions of the board, according to the evaluation of the cost benefit of such measures
- The implementation or revision of the formal performance evaluation of management and the board of directors
- The establishment of internal rules for evaluating the management and the board of directors
- The highest and lowest remuneration must include notes to financial statements.

Basic Principles of Corporate Management of State Companies in Bulgaria

Velichka Dimitrova Nenova[8]

1. Current State of PSEs

In the ranking list of the Top 100 most profitable companies in Bulgaria for 2010 are 14 are state companies, with regard to two key indicators – operating revenue and net financial result after tax. This group consists of mainly energy and transport companies.

State companies reported significantly more successful financial results for 2010. Transport companies narrowed their losses while energy companies greatly increased their profits from the previous year. At the same time both show an increase in revenue, which continued throughout the first half of 2011.

The strong financial results of the largest state companies mean a significantly higher dividend for the state.

The total amount of privatised fixed assets amounts to 65.49% – compared to the amount of all state assets at book value at 31.12.1995 and represents 99.18% of the fixed assets designated for privatisation.

The state has withdrawn from participation in economic life by state companies except in the sectors of energy and transport. In these sectors PSEs operate along with private companies.

Strategic goals are approved by the Council of Ministers and adopted by the National Assembly of Bulgaria.

Regarding the development roles, the public sector contributes to the development of the production of electricity (nuclear power), gas supply, railway transport, ports (river and sea) and airports. The private sector contributes to the distribution of electricity, power generation from renewable energy resources, air transport and road transport.

Bulgaria's act on commerce recognises only two legal forms of state-owned companies – joint-stock companies and limited liabilities companies:

Joint-stock company (JSC): a company whose capital stock is divided into shares. The company (not the shareholders) shall be liable to its creditors with its assets. All shares can be possessed by a single legal entity – in our case – the state.

[8] State Expert, Ministry of Economy, Energy and Tourism

Limited liability company (LLC): may be formed by one or more persons who shall be liable for the company's obligations with their contributions to the company's registered capital. It blends elements of partnership and corporate structures.

A joint-stock company is characterised according to its corporate structure, by a legal entity and unique name registered under the Commerce Register and by centralised management under a board structure. Its existence does not depend on membership. It has limited liability and transferable shares. They may be "public" (shares traded on the stock exchange) or closely (privately) held (traded by private placements). The single owner is registered in the Commerce Register. Its multiple shareholders are not registered.

Organs of a JSC are the general meeting of shareholders/single owner and the board of directors (in a one-tier system), or the supervisory board and the management board (in a two-tier system).

A list of issues taken into consideration and actions in a general meeting of shareholders/single owner:

- Amends the Articles of Association
- Resolves either increases or reductions of the capital stock
- Decides on the transformation and dissolution of the company
- Elects and recalls the members of the board of directors, or of the supervisory board as the case may be
- Determines the remuneration of the members of the supervisory board, or of the board of directors
- Appoints and dismisses registered auditors
- Approves the annual financial statement as audited by the appointed registered auditor, decides on profit distribution and the payment of dividend
- Resolves the issuing of debentures
- Appoints liquidators upon dissolution of the company, except in the event of bankruptcy
- Relieves of responsibility of the members of the supervisory board and managing board, or of the board of directors
- Resolves other matters which by virtue of the law or the Articles of Association are in its competence

Two particularly important issues:

Approving the annual financial report: In Bulgaria reports are audited by an independent auditor, or in the case of energy companies by a respected international auditor, selected for this purpose.

Relief of the responsibility of the members of the supervisory and managing boards: This is important because in Bulgaria members of the managing board give guarantees of their management (the amount of three months of salary).

Limited liability companies have some similarities with joint-stock companies:

- Both types of companies are separate legal entities which have their own privileges and liabilities distinct from those of their members.
- Creditors are granted (as opposed to shareholders) priority over the company assets upon liquidation or insolvency.
- Corporate assets cannot be withdrawn by the company's shareholders/partners, nor can the assets of the company be taken by personal creditors of its shareholders/partners.

Conversely, they also present key differences:

- A minimal amount of capital is required by law.
- All partners (one or several) are registered.
- Each partner is entitled to take part in the management of the company.
- Manager/managers structure instead of board structure
- The general meeting of partners is entitled to resolving additional monetary contributions, admitting and expelling partners, giving consent on the transfer of an interest to a new partner, deciding to on set up or close down its branches and participation in other companies and making resolutions on the acquisition or alienation of real estate/property.

2. Concluding Remarks and Future Prospects of PSEs

Regarding the organisation of state ownership functions in Bulgaria, the Council of Ministers or the Ministers (according to their branch competence) are entitled to exercise the rights of the owner of shares.

In a single person joint-stock company and a single person limited liability company, the single owner of the stock shall decide on issues within the competence of the general meeting.

On the basis of the Bulgarian experiences with the performance of public enterprises, some legal changes are conducted. The following activities require ministerial permission:

- Disposal of the fixed assets
- Rent of properties
- Acquisition or disposal of shares
- Mortgage and pledge of fixed assets
- Conclusion of agreements which recognise obligations or release debt

Election and nomination of management is within the competence of the government. Usually elections are done among several candidates. For example, in 2011 the director of the national energy company was elected after the publicly announced election.

Incentives and remuneration of the supervisory and managing boards are not fixed in Bulgaria. It is determined every three months, depending on the value of the fixed assets, stuff number of the company, profitability, financial results, service of liabilities, as well as all specific commitments in their contracts.

Evaluation of performance in SOEs is done in accordance with the fulfilment of the business programme of the company and the financial result. The Business Program is prepared by the management for a period of three years and contains specific indicators, as well as optimistic, realistic and pessimistic points of view. The Minister accepts the value of each indicator, and these values are compared with results achieved by the management at the end of the financial year.

Public Sector Enterprises (PSEs) in Egypt: Present and Future

Dr. Ashraf Hassan Abdelwahab[9]

1. Historical Background

Starting in 1952, Egypt adopted a communist regime and state-owned enterprises emerged. In that period state-owned enterprises represented the core economic backbone of the Egyptian economy. They were governed by the Nationalisation programme and specific legislation and were wholly owned by the government.

Egypt went through a thorough review of its economic structures in the mid 1980s which also provided reflection on the state-owned companies' business and their governance. The Egyptian Government implemented two main programmes aiming to restructure the financial sector while at the same time make the public sector more effective, and with this shift alter the ownership function and improve management.

The 1991 shift in Egypt's economic vision was to turn these companies into holding companies. The new Law No. 203/1991 on PSEs adopted in 1991 introduced the following basic principles:

- Establish state-owned holding companies (owning and not managing).
- Establish affiliated companies where the holding company owns 51%.
- Set rules and criteria for the selection of companies' management boards (holding and affiliated).
- Monitor through periodical reports to the Cabinet of Ministers on the companies' activities.
- Give the right to the holding and affiliated companies to develop their own administrative regulations.
- Determine an auditing unit inside the companies (holding and affiliated).

[9] Acting Minister, Ministry of State for Administrative Development, Egypt

By applying the Law, 314 public companies were transformed into 9 holding companies in 9 sectors. The Law also regulated how these holdings operate. On the other hand, holdings were given full authority and autonomy to follow their best course towards effective management.

The privatisation programme started to emerge in 1993, and, parallel to economic reform, it reduced the number of PSEs from 314 to 147 by 2011. However, the privatisation programme was highly criticised for several reasons, including a lack of transparency (companies' selection, pricing standards, boards, etc.), miscommunication of policies, lack of experience, improper distribution of returns contributing to unemployment, and corruption. Also, one of the critics addressed the lack of any tangible contribution to the national economy in terms of productivity or employment.

2. Current State of PSEs

Nowadays, three main categories of companies that are not subject to privatisation exist:

1. Certain public sector companies will not be privatised which are strategic for the government among five sectors: Media, General Authority for Oil, Suez Canal Authority, Banks and Arab Contractors Company.

2. Among public sector enterprises are 9 Holding Companies which hold the remaining 314 companies in various industries: Cotton, Spinning and Weaving; Metallic Industries; Chemical Industries; Pharmaceutical; Food Industries; Construction and Development; Tourism, Hotels and Cinema; Insurance; Maritime and Land Transportation.

3. Utilities holding companies for electricity, water and sewage are to be regulated but are not now to be privatised.

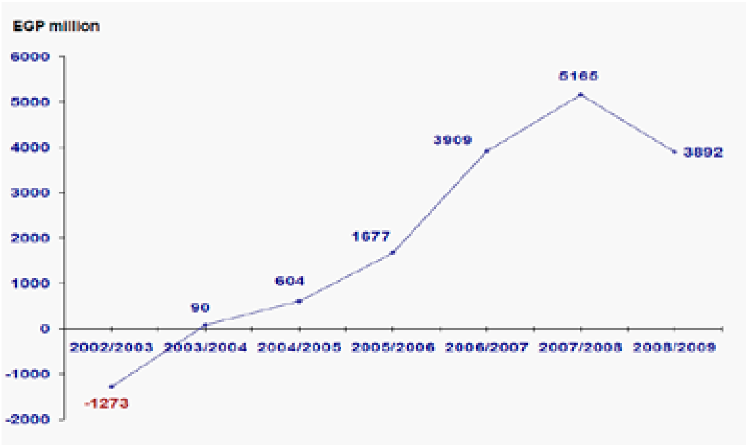
Main indicators of PSE performance in recent years are presented in Table 1

Table 1 – Main indicators of Egyptian PSEs

	03/04	04/05	05/06	06/07	07/08	08/09	09/10
Number of Affiliate Companies	174	166	164	163	155	150	147
Number of profitable companies	118	105	109	112	114	104	110
Number of companies showing losses	56	61	55	51	41	46	37
Operating Revenues *(EGP Million)*	39,907	43,421	44,305	52,190	61,233	61,500	64,400
Net Profit *(EGP Million)*	90	604	1,677	3,909	5,165	38,92	4,900
Total Salaries *(EGP Million)*	5,161	5,442	5,756	6,458	6,991	7,481	___
Number of employees	410,463	401,059	374,396	357,249	337,022	325,364	___

In addition, PSEs on an aggregate level came from making business losses to the zone of profitability; the profit trend is presented in Figure 1.

Figure 1 – Public Sector Enterprises' Net Profit



The main idea of Law 203/1991 is to give companies more autonomy in making decisions irrespective of the government and political will so that they are not in the chain pursuing different, maybe conflicting, policies and economic requirements, much as holdings have the authority to own a company but not to manage it.

3. Concluding Remarks and Future Prospects of PSEs

Theoretically, the possible company structures should improve the mechanisms for their management, but in practice this does not apply for various reasons:

1. Lack of vision & strategic coordination of socio-economic objectives

2. Lack of transparency and accountability: no criteria in selecting management, investors, boards of directors, pricing systems; miscommunication of policies to citizens in line with privatisation; misuse of liabilities, e.g. selling property to show profit without adding value to the economy, and the existence of only one auditing body (difficult to audit, facilitates corruption)

As a result, people do not feel any improvement in the economy. Another factor is the inherited cultural perception that government is responsible for providing subsidized goods and employment throughout this sector.

During the 25 January 2011 revolution, society was calling for employment and social justice; Egypt has adopted a new strategic vision for PSEs. New governmental strategy for public sector enterprises allows that they would be used not only as a part of the economy but as a major pillar in social-economic development, i.e. employment and the capacity and capability of government to intervene to ensure social justice.

The current plan of action, in line with the newly adopted strategy, includes the following elements:

- Termination of all privatisation processes
- Preparation of a complete strategic plan for public sector companies to be implemented according to a determined schedule
- Application of good governance principles
- Establishing new criteria for the selection of companies' management boards and members
- Tighten control , monitoring and accountability
- Re-engineering the companies' organisational structures

At the end of the day when talking about PSEs, it is always about Why and How? From Egypt's standpoint, here are some answers to these questions:

Why do we need to keep these companies and their benefits to the state? – They are necessary to support political vision and clear public policy on their role in society and to gain balance between commercial and social objectives.

How do we run these enterprises 'right'? – It is possible through good governance (transparency, ownership, accountability, etc.), expertise and access to finance.

Public Sector Enterprises – the Georgia Case

Gengiuri Vakhtang[10]

1. Historical Background

After the collapse of the Soviet Union, the state enterprises were operating in a different form and were managed by different line ministries, such as the Ministry of Economy, Ministry of Agriculture, Ministry of Transport and Communication and the Ministry of State Property Management. At the end of the 1990s, a law was established which regulated the form of state owned enterprises, and they were defined only as LTD. or JSC.

In 2003, the LEPL "Enterprise Management Agency" was created, and all state enterprises were transferred under its management. The LEPL "Enterprise Management Agency" conducts its activity according to the Georgian "Law on Entrepreneurship".

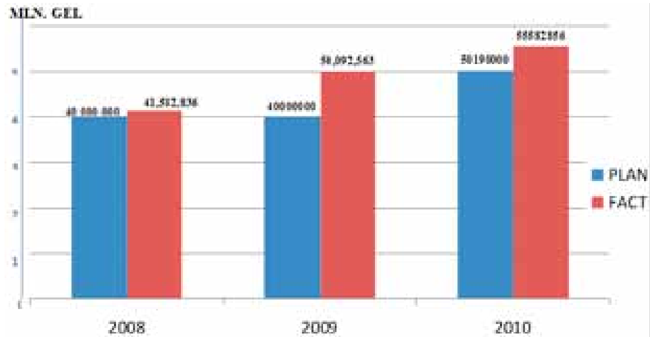
2. Current state of PSEs

Public enterprises are included in the national development strategy of the following sectors, such as the Transportation (Ltd Georgian Railway, Ltd Marabda Kartsakhi Railway, Ltd Union of Georgian Airports, Ltd Georgian Air Navigation), Healthcare, Energy, Agriculture and Communication (Ltd Georgian post) sectors.

In 1,136 enterprises 42,757 people are employed. Among them 317 enterprises are important (will remain under state management) and their revenues contribute 160,250,623 Gel. The remaining 819 enterprises are either in liquidation or in bankruptcy processes, and some of them need to be merged or will be transferred under the management of local government. Dividends gained in the last three years are shown in Figure 1.

[10] Head of Administration, LEPL Enterprise Management Agency

Figure 1 – Dividends of the Year 2008 – 2010



Strategic Goals of PSEs are determined by the Government of Georgia together with the line ministries and by the commissions created with the participation of corresponding ministries, such as the commission for discussion proposals concerning distribution and use of net income of the enterprises created by the state share participation and the commission for working out the Transportation and Communication Sector Development Policy of Georgia.

The LEPL "Enterprise Management Agency" closely cooperates with the private sector and implements mutual projects in the fields of Transportation, Healthcare and Agriculture.

According to the Georgian Constitution, the Ministry of Economic and Sustainable Development is determined as the successor of the property of the Ministries of Transport, Construction, Communication and State Property Management, and LEPL "Enterprise Management Agency" implements the rights of partner (share holder) within the state enterprises.

State ownership functions are exercised by the Privatization Department, State Property Management Department of the Ministry of Economic and Sustainable Development of Georgia and by the LEPL "Enterprise Management Agency" which conducts its activity according to the Georgian Law on Entrepreneurship and its main function is implementing the rights of partner (share holder) within the enterprises created by the state share participation, with the exception of the rights of privatization or disposal of shares and stocks being under state ownership.

For evaluation of PSEs different types of methodologies are being used, such as qualitative and quantitative research, and the data are compared to the previous years' results in order to give a more or less exact picture to define the successive enterprise. According to this methodology in different nominations, 12 companies were selected which represent the different fields of activities.

3. Concluding Remarks and Future Prospects of PSEs

In regard to the future activities, there are three steps to be conducted:

1. Registering the enterprises and their assets which encompasses the following activities:

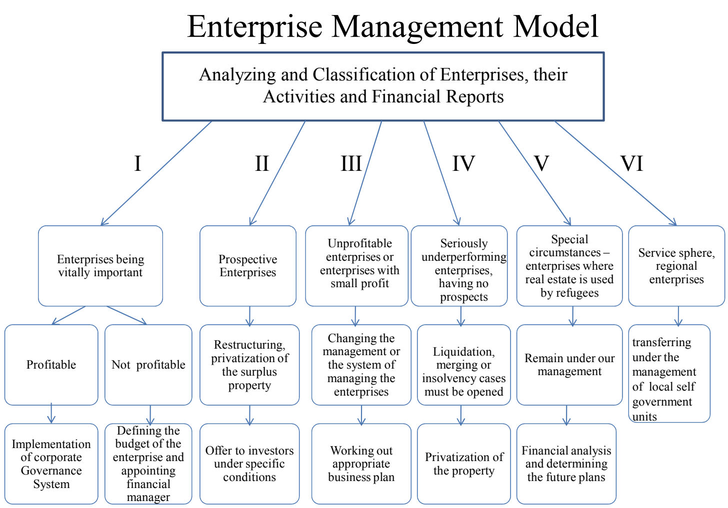
    - Comparison of the Agency's information with the information of the Business Register and territorial units of Ministry of Economic and Sustainable Development of Georgia
    - Requiring the renewed documentation from enterprises is necessary (Balance and profit-loss list) for analyzing profitability and solvency of enterprises and also to ascertain their liquidity (gives us the opportunity to classify enterprises by basic categories).
    - Registration of the property of the enterprises and Creation of exact real estate data; (gives us the possibility to make corresponding decisions regarding the enterprises classified by categories)

2. Classification of the enterprises into several basic categories

3. Adoption of the corresponding decisions regarding the enterprises divided into categories

Classification of public enterprises in accordance with the Enterprise Management Model is given in Figure 2.

Figure 2 – Enterprise Management Model



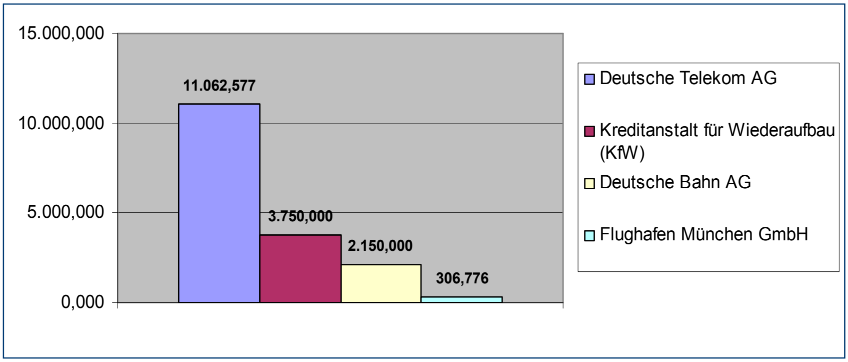
State Ownership in Germany – Holding and Privatisation Policy of the Federal Government

Dr. Michael Offer[11]

1. Current state of PSEs

Due to a longstanding privatisation policy, the total number of 87 direct holdings and 20 holdings of special funds owned by the federal government could be considered to be quite small. The portfolio of direct holdings is dominated by a few state-owned enterprises (Figure 1). Some holdings are left from former times, such as Treuhandanstalt, or the current Federal Agency for Financial Market Stabilisation, founded in 2008 as an instrument for resolving the financial markets crisis. These are special types of agencies because their purposes refer to specific economic sectors as a whole, and not – as holdings in general – as instruments to fulfil specific tasks. For example, the Federal Agency for Financial Market Stabilisation administers the Financial Stabilization Fund and its instruments for stabilising and restructuring financial institutions being affected by the financial market crisis. With this, the government became a shareholder of two large banks.

Figure 1 – Largest Direct Holdings; grading according to nominal capital (in million Euro)



Clear Separation of Government Instruments

Holdings, predominantly in the legal forms of private law (Figure 2), are government instruments much as others like regulation or granting subsidies. The Federal Budget Code is quite restrictive and states that the government should participate in the

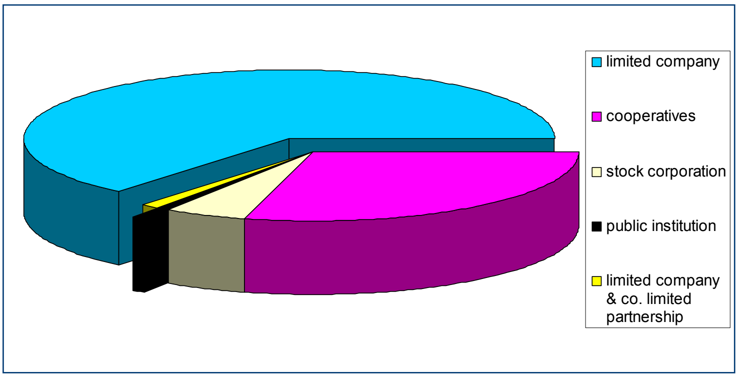
[11] Head of Directorate VIII B, Ministry of Finance

founding of a private-law enterprise or in an existing enterprise only if there is an important interest on the part of the federal government and that the purpose intended by the federal government cannot be achieved better or more economically in any other way. The background rationale of this restrictive approach is to avoid an evasion of federal government administration into legal forms of private law.

Functional separation of government instruments for more efficiency should lead to several consequences:

- within the government – separation of government function
- within the market – competitive neutrality
- within the enterprise – avoiding conflicting objectives

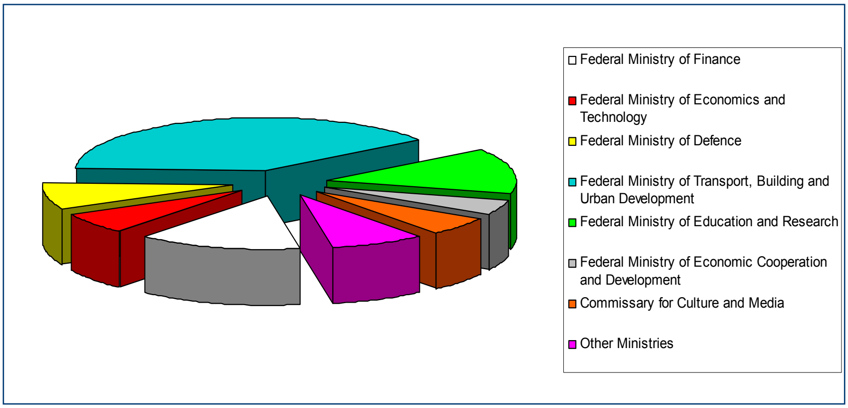
Figure 2 – Direct Government Holdings, divided according to legal form



Organisation of State Ownership

Germany has a dual model of holding administration which is close to a decentralized sector model (Figure 3). Sector ministries exercise the ownership function, e.g. representing the state in the general assembly of shareholders, and have responsibility for determining or influencing the strategic goals of federal government holdings as well as for the practice of corporate governance of their holdings. Even though these ministries exercise the ownership function, management boards are responsible for achieving the goals of government holdings. Determining strategic goals is part of the ownership function the sector ministries execute, partly in coordination with the Ministry of Finance when setting up the company or changing elements of the articles of association which, for example are relevant for the budget or concern the influence of the federal government.

Figure 3 – Direct Government Holdings, divided among Sector Ministries



Besides exercising the ownership function for some holdings as a sector ministry, the Federal Ministry of Finance has central tasks concerning the corporate holdings policy of the federal government. These tasks, separated from the ministerial responsibilities for the holdings, may include setting standards for the administration of government holdings, like the Public Corporate Governance Code and administrative guidelines. Furthermore, approval of the Ministry of Finance is obligatory for setting up government holdings by sector ministries.

Exercising Influence on Government Holdings

The federal government has no "golden shares"; it has the same rights as every shareholder. Consequently, using holdings as an instrument includes in most cases a majority stake of 100% ownership by the government. The government exercises its necessary influence in three ways:

- the formulation of the articles of association
- the general assembly of shareholders and informal discussions
- the supervisory board members the government can influence

Exercising influence on the supervisory board is a key tool for administrating government holdings because the supervisory board has a close relation to the management board. Influence is exercised by board members being sent to the board or elected by the general assembly of shareholders. Board members may be public servants of the holding administration or experienced private sector managers.

2. Concluding Remarks and Future Prospects of PSEs

As far as government holding policy is concerned, the focus is on more professional administration and governance of corporation holdings which include a regular review of the Public Corporate Governance Code and training for supervisory board members of the federal government. Concerning privatisation policy, the Federal Budget Code is a guideline for further action: the privatisation process of state-owned enterprises shall be initiated once any important federal interest is no longer given. In doing so, a framework of conditions need to be considered to allow privatisation at an appropriate price.

The current theme is The Grandhotel Petersberg, illustrated in Box 1.

Box 1 – Proceedings initiated to sell Grandhotel Petersberg

The Grandhotel Petersberg is the former German government guest house located in an exclusive area near Bonn; it is world renowned and highly prestigious.

The property is owned by the Bundesanstalt für Immobilienaufgaben ("BImA" – Federal Institute for Real Estate Business). The use of the property has been ceded to the Gästehaus Petersberg GmbH (owned by the Federal Ministry of Finance).

The Gästehaus Petersberg GmbH has signed a medium-term management contract including a guaranteed minimum return with the Steigenberger Hotels AG. The Steigenberger Hotels AG operates the property as a Grandhotel.

The Federal Ministry of Finance and BImA have jointly initiated a privatisation process for the sale of the Gästehaus Petersberg GmbH and the "Petersberg" property in order to sell the two in a transparent and competitive process.

Hungarian State Holding Company: Governance of State Ownership

Dr. Csaba Polacsek[12]

1. Historical Background

State-owned companies have a significant effect on Hungarian GDP, thus state ownership plays an important role in the Hungarian economy, and it is a significant tool in executing government public policies.

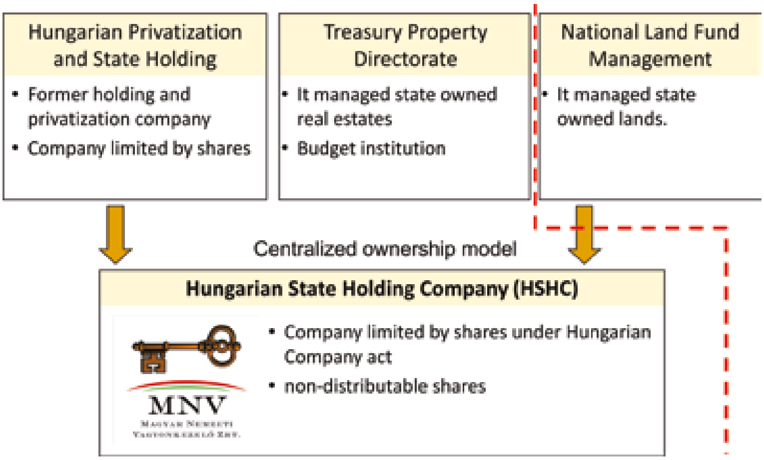
After the socialist regime, privatisation started without any strategic thinking of future state ownership arrangements, and it came to an end relatively early. Bad governance practices in the management of the remaining state-owned assets', i.e. corruption, were in the limelight. In order to be a responsible owner, the state placed new focus on good governance and accountability, based on the application of private equity best practices, which is a must when it comes to state-owned asset management.

Asset management – and within this the regulation of state assets and supervision of their ownership – falls within the Ministry of National Development's remit. The Hungarian State Holding Company (HSHC) was established to improve the reputation of state-ownership and to expand business-oriented thinking and management.

The establishment of HSCH as part of the national asset management framework was the result of moving the execution of state ownership rights towards a centralised model, which is presented in Figure 1.

[12] Deputy CEO, Head of Corporate Portfolio, Hungarian State Holding Company

Figure 1 – Hungarian State Holding Company: moving towards the centralised model



2. Current State of PSEs

Besides the Hungarian State Holding Company, two different ownership entities remained, as presented in Table 1.

Table 1 – 3 different ownership entities

Hungarian State Holding Company	• Majority-owned companies in different sectors, e.g. energy, postal, lottery, transportation, etc. • Several minority shareholdings, including listed companies
National Development Bank	• Mainly financial or financial related companies • Other specific sectors, e.g. forestry and infrastructure
Entities declared by other law	• Specific and large companies • Their ownership entities are mainly ministries

The structure of state-owned companies included in the HSCH portfolio is presented in Table 2.

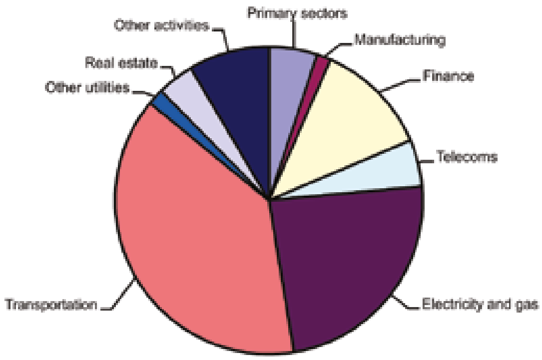
Table 2 – Structure of HSCH SOE portfolio

HSCH SOE portfolio	number
companies	**415**
managed directly by HSCH	**358**
functioning companies	**214**
-majority owned	124
-minority owned	90
under voluntary dissolution	***60***
under liquidation	***84***
managed by other entities (asset management contracts)	**57**

Regarding the HSCH portfolio, several important facts should be emphasized:

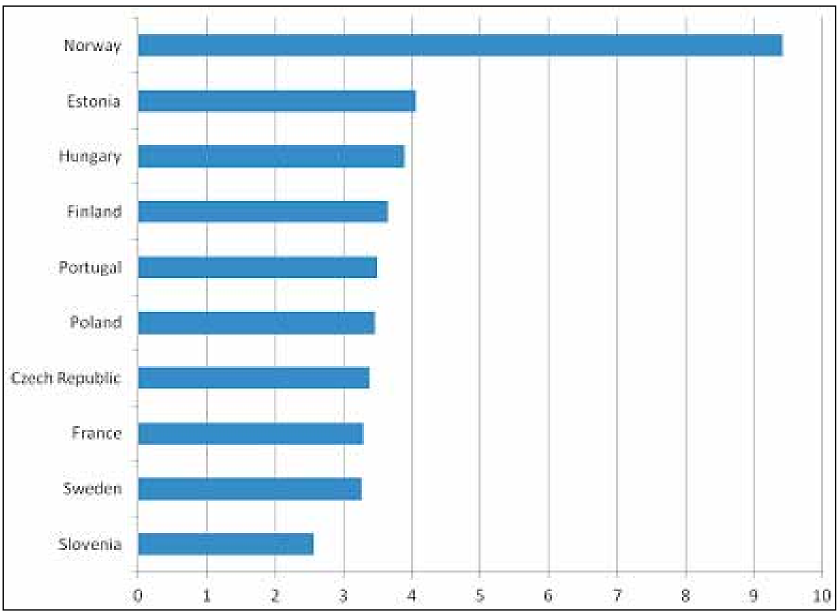
- Functioning companies have a total balance sheet of €10.4 billion in proportion to HSHC ownership.
- Total book equity value of the majority-owned HSHC SOE portfolio is €5.6 billion.
- In regard to the breakdown by sector of total asset value of majority-owned SOEs, the transportation and the electricity and gas sectors have the largest participation.
- Non-homogenous portfolio
- HSHC has the right to deal with inherited companies.
- HSHC liquidates companies that have no future perspective.
- 14% of the state's real estate is directly managed by HSHC (total real estate value is €31 billion).

Figure 2 – Total assets of majority-owned SOEs – sectoral breakdown in 2011



In addition, the SOE sector is a significant employer. International comparison of SOE employment across several European countries is presented in Figure 3.

Figure 3 – SOE employees as % of total employment in 2010



In terms of state ownership policy adequacy, the following important lessons have been learned:

- Deciding what level of state ownership is adequate should be part of the national strategic thinking.

- Regarding controlling market failures and anomalies in smaller states, ownership position is more important than regulatory position.
- Via an ownership position, policy makers will have better access to market information and 'drivers' of pricing.
- 'Spontaneous privatisation' (without any strategic considerations) is one of the biggest problems in Hungary.
- Foreign background multinational companies channelled their profit out of Hungary (low profit reinvestment level).
- Keeping the natural monopolies (water supply, electricity, gas supply) with state-controlled ownership would have been important.
- Delivering quality public services is easier when the state has a strong ownership position.

The implementation and monitoring of commercial and non-commercial objectives is based on the following principles:

- Commercial and non-commercial activities are divided and accounted separately.
- Non-commercial public benefit activities must be in line with the company's articles of association.
- Subsidies must comply with EU state-aid regulation.
- Nonprofit business associations may engage in business operations only in the form of ancillary activities.
- The State Aid Monitoring Office has the task of ensuring that state aid in Hungary is granted in accordance with EU regulation.
- Strict policies to avoid overcompensation of non-commercial activities must be in place.

3. Concluding Remarks and Future Prospects of PSEs

Hungarian state-owned asset management accepts and applies international asset management best practices, continuous development of national asset management practices and centralised asset policy at the ministry level with more ownership exercising institutions.

In defining the asset management strategy, several important remarks have been put into consideration:

- Instead of administrative management the focus is to create the framework for business-oriented asset management.
- Goals to fulfil during asset management are effectiveness, making economic value-added decisions and being cost sensitive.
- The main focus is to reinforce accountability and corporate governance.
- Strategic thinking at the operational level is a necessity.
- Before setting a comprehensive strategy there were alarming issues to address:
    - Due diligence of companies
    - Replacing management at SOEs where necessary
    - Understanding the contractual frameworks of SOEs (especially long-term commitments).

Table 3 – Critical strategic points

Strategic points	Target
Individual company strategies	• Strategy is a basic document • Strategy is based on the business model of the company
Business-oriented approach	• Mining out possibilities • How to find solutions
Risk management	• Risk map • Risk management system
Corporate governance	• Broad corporate governance recommendations • Roles and responsibilities of management

There are several further steps to improve governance:

- Developing sustainable and measurable business models
- Structures built on portfolio synergies
- Portfolio clean-up

- Corporate governance check list for SOEs

In addition, two examples of state asset management are presented in Box 1 and Box 2, respectively.

Box 1 – Example of real estate management

The Palace is one of the most important, largest monuments of Hungarian Palace architecture. Its builder, Count Antal Grassalkovich I (1694–1771) was a typical figure of the regrouping Hungarian aristocracy of the 18th century. He was a Royal Septemvir, President of the Hungarian Chamber, and confidant of Empress Maria Theresa (1740–1780). The construction began around 1733, under the direction of András Mayerhoffer (1690–1771), a Salzburg builder.

In 2009, an enormous renovation project was launched in order to restore the major part of the building that will serve as the most important summit building during the Hungarian EU Presidency in 2011.

Box 2 - Example from the company portfolio

MVM Group:

- #1 electricity power generator in Hungary
- #1 wholesale electricity trader in Hungary
- 99,9% owner of the Hungarian power grid company

	2009	2010
Number of employees	8 534	8 090
Revenues	€ 2 144	€ 2 083
EBITDA	€ 431	€ 418
Profit before tax	€ 315	€ 306
Net profit	€ 225	€ 218
Total assets	€ 3 008	€ 2 923
Equity	€ 1 809	€ 1 757

Policy for Effective Management of State-Owned Enterprises in Latvia

Juris Puce[13]

1. Current State of PSEs

In Latvia issues regarding the state ownership function and SOEs are in the competence of the Cabinet of Ministers. Such tasks are defined in policy documents and strategies (Strategic Development Plan 2010–2013, Declaration of the Intended Activities of the Cabinet of Ministers, etc.)

Main sectors where SOEs operate are energy, telecommunications, forestry, transportation, real estate, health and others.

By Latvian law the state may engage in business only in the following cases:

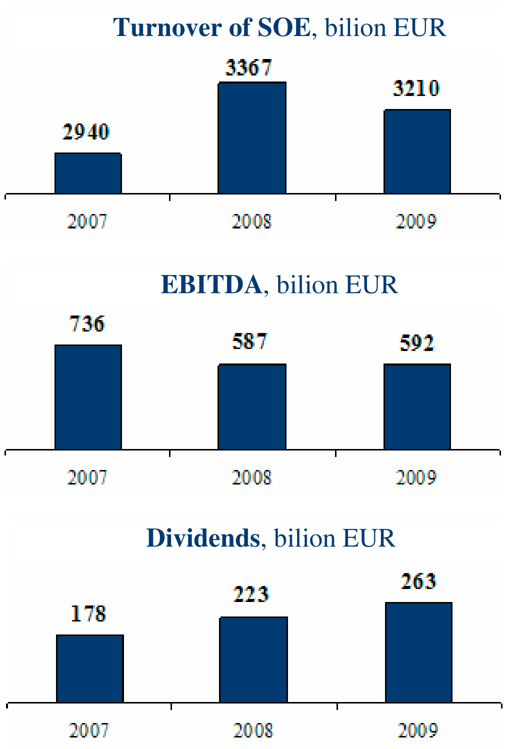
- The market is unable to ensure the collective interests of society
- Industries holding natural monopolies
- Strategically important industries
- New industries
- Capital intensive industries
- Industries with the need to ensure the highest quality standards

Latvia is a shareholder directly and indirectly in more than 140 enterprises, including 74 fully owned (from Latvenergo with a turnover of EUR 712 million to the National Symphony Orchestra). The majority of them are leftovers of the big process of privatisation, as 95% of the companies in Latvia were state owned at the beginning of the nineties.

More than 52,000 people were employed in SOEs (5% of the national total employed). At the end of 2009, total assets of SOEs amounted to EUR 10.17 billion, with combined turnover of EUR 3.2 billion (17.2% of GDP). The average net profit margin was 5.9% in 2009. EBITDA is resilient even in crisis, and dividend flow is low but steady. The most important financial data on Latvia's SOEs for the period 2007–2009 are given in Figure 1.

[13] State Secretary, Ministry of Economics

Figure 1 – Financial data on Latvia's SOEs



The main issues addressed:

- Governance is decentralised – managed by 11 line ministries.
- Government is extensively involved in SOE governing, including significant political influence over operational decisions.
- Lack of a business oriented approach – unbalanced sector policy implementation and commercial perspective
- Low return on invested capital – total return on equity of SOEs, excluding the financial sector, was 7% in 2009
- No goals are set for measuring SOE performance
- Non-transparent and not very professional supervision

- SOEs which act as public state agencies

2. Concluding Remarks and Future Prospects of PSEs

Key reforms up to 2013 include two major strategy roles:

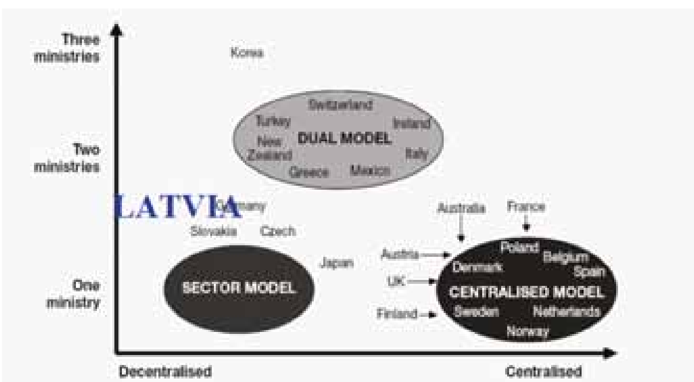
Reassess the principles for engagement of public persons in business activities. The main idea is to reorganise SOEs that are performing only public administrative functions into public state agencies and to decrease public sector engagement in business when there is an obvious market failure addressed to government ownership.

Implementation of OECD corporate governance principles:

- Setting up a centralised SOE manager (status, functions)
- Measuring SOE performance (currently decentralised management by line ministries; a common reporting system pilot project is ongoing)
- Ensuring transparency on state capital activity
- Revising dividend policy
- Reviewing supervisory board institute (does not exist for limiting political influence)
- Re-evaluating remuneration policy

Latvia intends to move towards a centralised ownership function, but ownership is currently organised in respect to a dual model, as presented in Figure 2.

Figure 2 – Position of Latvia's ownership function regarding the OECD countries



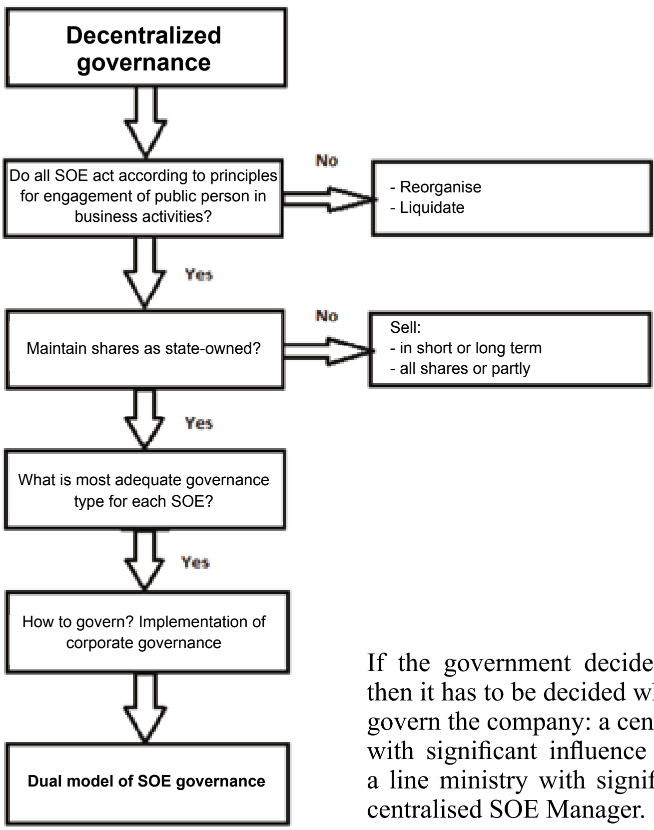
The functions of the centralised SOE management institution that is planned to be established in Latvia are presented in Table 1.

Table 1 – Functions of the SOE Manager (to be adopted)

Implementation of **corporate governance principles** and improvement of governance practice	Ensure **information transparency** regarding use of state capital	**Advise government, line ministries, SOE** on corporate governance
	CENTRALISED SOE MANAGER	
General supervision of SOEs and disposal implementation	Definition of specific, measurable **business objectives** (economic and social); an annual evaluation of the results achieved	Provide **regular assessment on** whether to maintain state ownership of shares of a particular SOE

There are 4 decisions to be taken on each of the companies (presented in Figure 3)

Figure 3 – Decisions to be taken within SOE government reform



If the government decides to maintain shares, then it has to be decided which institution should govern the company: a centralised SOE Manager with significant influence of a line ministry or a line ministry with significant influence of the centralised SOE Manager.

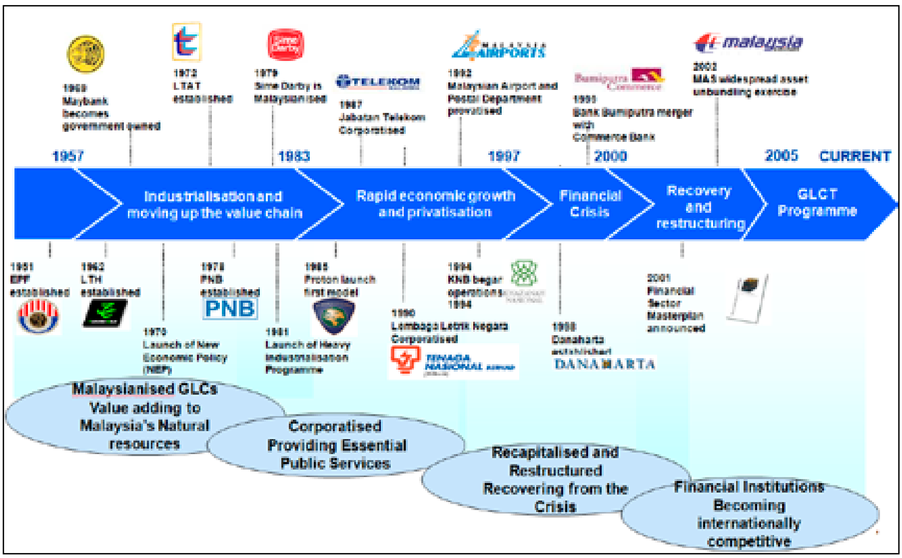
Government Linked Companies Transformation (GLCT) Programme

Abdul Aziz Abu Bakar[14]

1. Historical Background

Government Linked Companies (GLCs) are an integral part of the Malaysian economic engine. They provide mission critical services and catalyse developments in strategic sectors. GLCs account for around 5% of the national workforce (400,000 employees). However, GLCs historically underperformed the broader Malaysian market, both financially and operationally. In 2004, the GLC Transformation (GLCT) Programme was launched with the dual aims of enhancing economic performance and accelerating the country's social and economic developments. The Programme only covers GLCs held by Federal Level Government-Linked Investment Companies (GLICs) that allocate some or all of their funds to GLC investments.

Figure 1 – History and evolution of GLCs

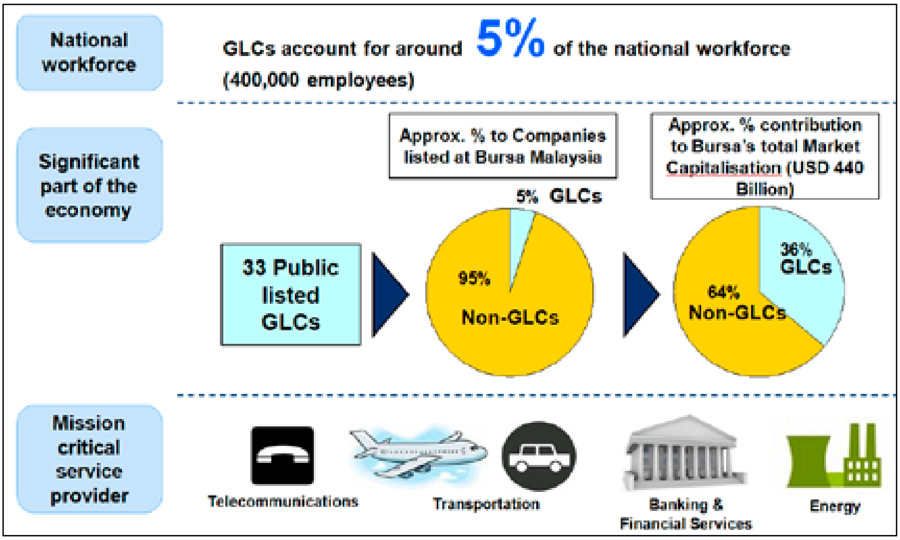


[14] CEO/ Executive Director, Malaysian Directors Academy

2. Current State of PSEs

GLCs are a main contributor to the country's development because they are the backbone and driver for most mission critical services, i.e. Financial services, Telecommunications, Transportation, Energy, etc. There are 33 publicly listed GLCs on the Malaysian Stock Exchange (5% of total listed companies) which have 36% of the total market capitalisation.

Figure 2 – GLCs Contribution



Underlying principles of GLCT:

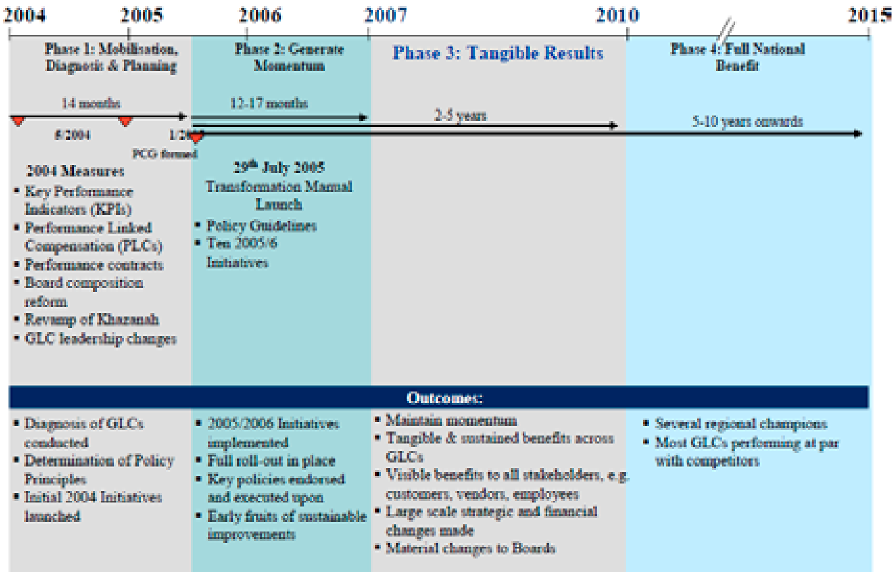
- National development foundation
- Performance focus
- Governance, shareholder value and stakeholder management

Five policy thrusts (below) and ten initiatives were identified based on extensive interviews, diagnostics and syndication:

- Clarifying the GLC mandate in the context of National Development
- Upgrading the effectiveness of boards and reinforcing the corporate governance of GLCs
- Enhancing GLIC capabilities as professional shareholders

- Adopting best practices within GLCs
- Implementing the GLCT Programme

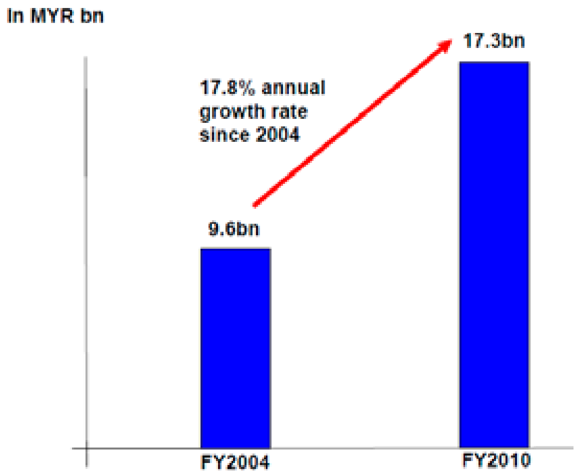
Figure 3 – GLC Transformation Programme in its 7th year



By 2006, all 10 GLCT Initiatives had been launched. They were published in ten books: Enhancing Board Effectiveness; Strengthening Directors' Capabilities; Enhancing GLIC Monitoring & Management Functions; Improving the Regulatory Environment; Achieving Value through Social Responsibility; Reviewing and Revamping Procurement Practices; Optimising Capital Management Practices; Strengthening Leadership Development; Intensifying Performance Management; Enhancing Operational Efficiency.

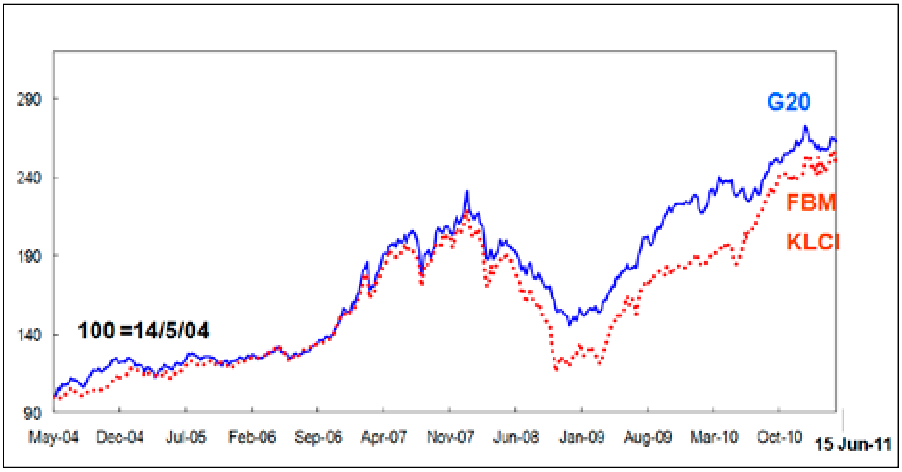
Since the GLCT Programme began in May 2004, the G20 (selection of originally 20 larger GLCs controlled by the GLIC) has shown significant tangible improvements in all key financial areas and successfully weathered the 2008/2009 Global Financial Crisis. FY2010 results indicate that the G20 is on a strong positive growth trajectory, and, indeed, key financial indicators for FY2010 such as revenue, net assets and dividends, now actually exceed their FY2007 highs.

Figure 4 – G20 Aggregate earnings



G20 (a selection of originally 20 larger GLCs controlled by the GLIC) total shareholder return grew by a compounded annual growth rate of 16% over the past 7 years, outperforming the Kuala Lumpur Composite Index (KLCI) by 2.1%.

Figure 5 – G20 total shareholder return



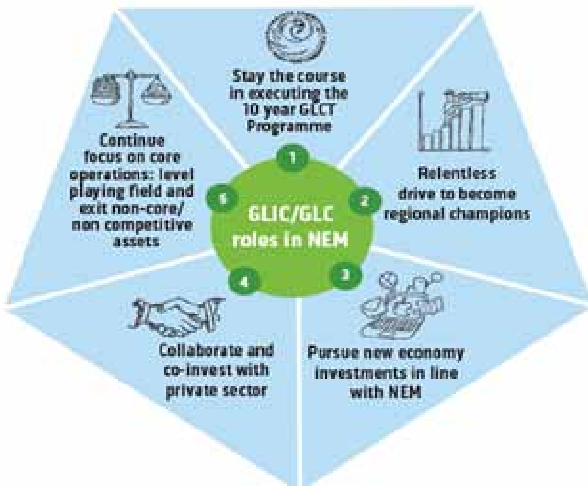
G20 total shareholder return grew by a compounded annual growth rate of 16% over the past 7 years.

It is also important to emphasize that the whole process had strong support from the Prime Minister of Malaysia who is also the Chairman of the Putrajaya Committee on GLC High Performance.

3. Concluding Remarks and Future Prospects of PSEs

The new Government and Prime Minister are very committed to ensuring GLCT continues to be implemented, if anything, with greater urgency and focus. GLCs must aspire to greater heights, whether best in class or emerging as future regional if not global champions. Malaysia launched a new economic model because reform of only the private sector or only bureaucracy is not enough, so the role of GLCs in the New Economic Model is crucial.

Figure 6 – 5 roles of GLICs and GLCs in the new economic model



Still, there are a lot of issues and challenges remaining in the development of GLCs and NEM. The massive gap in talent, execution skills and capabilities at GLCs is a consequence of brain drain during last decades, so the Government has established an agency (Talent Corporation Inc.) for contacting and attracting young talented people to return to Malaysia.

Philippine SOEs: Towards Higher Standards of Governance

Charissa P. Hipolito[15]

1. Current State of PSEs

The local term in the Philippines for SOEs is Government Owned or Controlled Corporations (GOCCs), which have at least 51% government ownership. Basically they are created and mandated to provide social services while generating profits to support their operations. GOCCs are recognised as significant tools for economic development and therefore generally serve as catalysts for economic growth and social development. They are considered also as the government's arm for implementing major projects the private sector is unwilling to undertake or where private interest is insufficient.

At present, around 157 GOCCs operate in key sectors of the economy – banking, pensions, transport, power, agriculture and housing. These GOCCs were created by a special law or referred to as chartered government corporations, while the others are created under the Corporate Code.

Based on the latest available data of audited reports, Table 1 gives the main financial data on Philippine SOEs sector.

Table 1 – Main Financial data on SOEs in the Philippines

Current Status as of 2009 (in Trillion Philippine Pesos)	Total Assets	7.19
	Total Liabilities	5.11
	Total Revenues	0.13
Contributions to Fiscal Consolidation Program 2005 – 2009 (in Billion Philippine Pesos)	Average Total Collections	29.5
	Average Dividend Remittances	10.3

In the Philippines, the role of the State as owner of GOCCs is exercised through the following channels:

- Board of Directors
- Supervising Department
- Oversight Agencies (Department of Finance (DOF), Department of Budget and

[15] Director, Department of Finance

Management (DBM), National Economic and Development Authority (NEDA), Bangko Sentral ng Pilipinas (BSP)and the Commission on Audit (COA))

- Office of the President

One of the key accomplishments in the Program of Reforms of the SOE sector was achieved through privatisation. Privatised GOCCs that have attracted a significant number of foreign and domestic investors are the Philippine National Oil Company-Energy Development Corporation (PNOC-EDC), Petron Corporation, Philippine Airlines and the Philippine National Bank. Privatisation reduced the number of SOEs from around three hundred in the 1980s to about 157 now.

2. Concluding Remarks and Future Prospects of PSEs

Key governance issues and challenges identified and experienced in governance of GOCCs:

- Lack of clear ownership policy of the State (there are many oversight agencies, thus a need to adopt clear ownership policy.)
- Conflicting mandates and multiple levels of oversight
- Need to strengthen board governance
- Need to strengthen transparency and disclosure standards
- Sustainability of financial and operational performance as well as service delivery
- Political interference in tariff setting (case of railways)
- Need to rationalise SOEs sector
- Need to instil fiscal discipline among SOEs
- Need to rationalise the compensation structure of board directors (already started)
- Removal of Charter provisions on automatic government guarantees
- Poor compliance to reportorial requirements

Regarding the abovementioned issues, there are several governance imperatives in managing GOCCs:

- Strengthen board governance (foundation of new administration, transparency in the selection process, professionalism and meritocracy, making the programme of board training mandatory, annual board evaluation).

- Update ownership policy (modification and codification of policy related to the SOEs sector and more unified application)
- Further rationalise the SOE sector (encourage efforts toward public private partnership, proactive management of contingent liabilities, etc.)
- Enhance transparency and disclosure practices (requirement to all SOEs to public data on their performance on the websites)

Within the process of Philippine SOEs reforms, the following comprise ongoing corporate governance initiatives:

- Pursuing corporate governance (CG) and continued improvement regarding the CG Scorecard
- CG Scorecard benchmarking
- Deepening CG reform by moving beyond compliance
- Institutional and financial reforms geared towards operational and financial efficiency

The future direction is closely related to the passage of the GOCC Governance Act of 2011 which is the basis for the creation of the Governance Commission for GOCCs (GCG). GCG is the central advisory, monitoring and oversight body with the authority to formulate, implement and coordinate policies for GOCCs. It is granted with powers and responsibilities to evaluate the organisational performance and compensation structure of GOCCs, mergers, privatisations and even the abolition of GOCCs. Abilities of the GCG as the centralised authority over SOEs:

- Review and update of government ownership policies
- Strengthen Board Governance
- Pursue further rationalisation of GOCCs
- Pursue strategic partnerships with development partners, the private sector, NGOs and other non-state actors
- Pursue a performance contracting system
- Strengthen Contingency Liability Management

20 years of experience with the transformation of state property to private property in Slovakia

Anna Bubenikova[16]

1. Historical Background

In the beginning of the 1990s, there were great expectations from the transition process and privatisation in Slovakia. This historical change in society was seen as a chance for the elimination of state dominance and the tool for increasing the efficiency of the national economy. A strong desire for prompt prosperity was present at the time. There was no question about whether to privatise or not, but how to do it: quick and massive privatisation or slow and steady.

According to the recommendations of international financial institutions, Slovakia chose the first way, conducting a quick and massive privatisation process. Slovakia used two approaches during the process, small and large-scale privatisation.

Small-scale privatisation
The process of small-scale privatisation was the transfer of retail and services providing companies' property to Slovak citizens. The method used in small-scale privatisation was public auctions, and the main goal was to create a small and medium enterprises sector.

Large-scale privatisation
The large-scale privatisation was more complicated and the more difficult part of the privatisation process. In 1991, the Government approved the list of state-owned companies to be privatised. Several methods were used during the large privatisation process: voucher privatisation, direct sales, public auctions and public tenders.

Voucher privatisation
This method was an experiment. The idea was to transfer a substantial part of state-owned companies to joint-stock companies, and then gradually hand over the shares to citizens as the investment vouchers. This type of privatisation brought along many risks. The property was atomized among the citizens, and the companies did not have any strategic shareholders that would force management to run the companies efficiently.

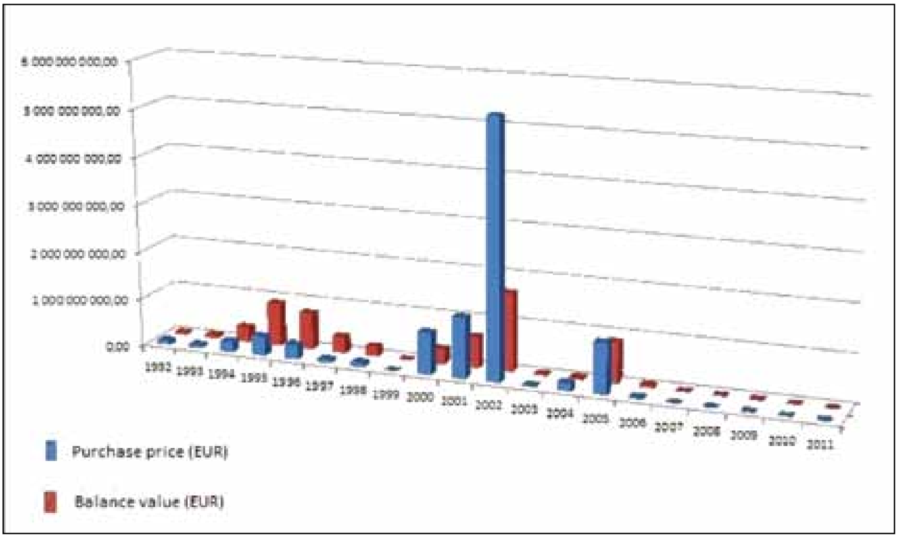
Eventually, the voucher privatisation fulfilled its objectives. The risk of corruption decreased and citizens participated in collective investment.

[16] Chairperson of the executive board of Fond of National Property

The privatisation process in the period 1994–1998

Following the voucher privatisation, direct sales and public tenders were organised, but exclusively for domestic investors. These government preferences towards domestic investors led to both decapitalisation and stagnation of efficiency and productivity in domestic privatised companies. As can be seen from the figure below, during the privatisation processes of direct sales and public tenders, purchase price did not play significant role.

Figure 1 – Purchase price and balance of value of privatised firms



During the period 1994–1998, the process of privatisation did not achieve the highest possible prices for the country's budget, and almost half of the privatised companies were liquidated or went bankrupt relatively quickly.

2. Current State of PSEs

Table below presents benefits from the privatisation process in the Republic of Slovakia, regarding the type of company ownership.

Table 1 – Benefits from privatisation

ownership	before transformation	after transformation	revenues from dividends	revenues from taxes	other benefits
100 % **private**	loss	profit	NO	YES	employment
100 % **state**	loss	x	NO	NO	potential source
state + stragegic investor	loss	profit	YES	YES	satisfactory purchase price

The process of managing the companies needs to be in accordance with corporate governance principles. Slovakia has managed to successfully implement the following CG principles:

Equitable treatment of shareholders

- Standard shareholder rights for the Fund
- Autonomous decision making for companies
- Protection of minority shareholders
- Selection procedure rules transparent on the website

Integrity and ethical behaviour

- Proved moral integrity

Interests of other stakeholders

- No privileged position
- Effective debt recovery for creditors
- No exceptions from the law

Responsibilities of the board

- Accountability of members
- Regular reports to shareholders
- Strategic, business and financial planning

Disclosure and transparency

- Collection of documents publicly accessible
- Remuneration disclosure
- Internal audit

3. Concluding Remarks and Future Prospects of PSEs

Slovakia has chosen an inappropriate method of privatisation. The process was characterised by weak institutional and legal framework. The preferences towards inexperienced domestic investors caused regular misuse of the situation.

The speed of the process must not have a higher priority than building solid institutional and legal framework, despite the pressures of international financial institutions, which proposed the quick and massive privatisation for Slovakia.

Much has been done on implementing the corporate governance principles. Readiness to face the constant tendencies to misuse the system must be the priority. The objective for the future is to establish and cultivate a system that will be able to react immediately to any such abuse.

Ownership Function and Strategic Management of State-Owned Enterprises in Turkey

Ayşe YİĞİT[17]

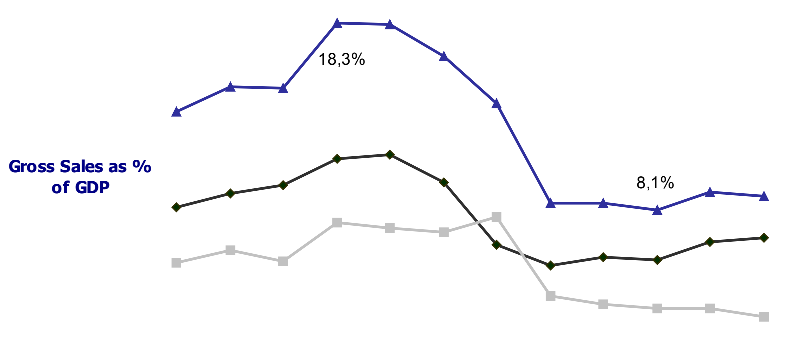
1. Historical Background

In the 1990s, Turkey had more than 60 different State-owned Enterprises (SOEs). They had a significant share of GDP and public investments, and 660,000 people were employed by these entities.

SOEs played a significant role in the Turkish economy up to the last five years. The share of SOEs in the Turkish economy has been declining with successful privatisations. Privatisation in Turkey not only aims to minimize the state's involvement in economic activities and to relieve the financial role of SOEs in the national budget, but also to contemplate the development of capital markets and enrich channels of resources towards new investors.

Today the number has been reduced to 27 SOEs, and they also have a lower share of GDP, public investments and employees (186,000 employees). This situation is a result of mergers and privatisations. From 1985 until today, total proceeds from privatisations are recorded as around US $42 billion.

Figure 1 – Significant drop in gross sales



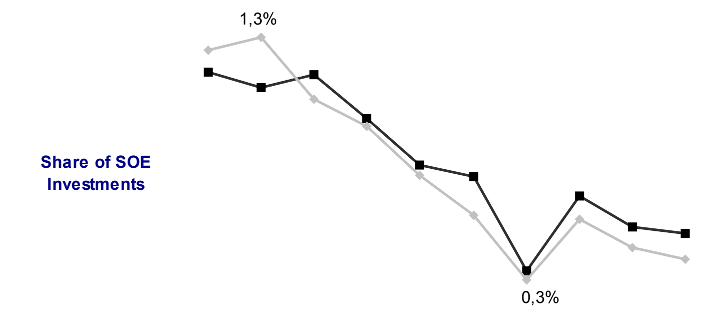
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Treasury P.	8%	9%	9%	11%	11%	10%	6%	5%	6%	5%	6%	7%
Privatization P.	5%	6%	5%	7%	7%	7%	8%	3%	3%	3%	3%	2%
Total	14%	15%	15%	18%	18%	16%	14%	9%	9%	8%	9%	9%

[17] Head of Department, Directorate General of State Owned Enterprises, Treasury

2. Current State of PSEs

The privatisation of SOEs also had a significant impact on the amount of investment by SOEs. SOEs made total investments as large as 1.3% of GDP in 2000 but only 0.3% of GDP in 2005, as shown in Figure 2.

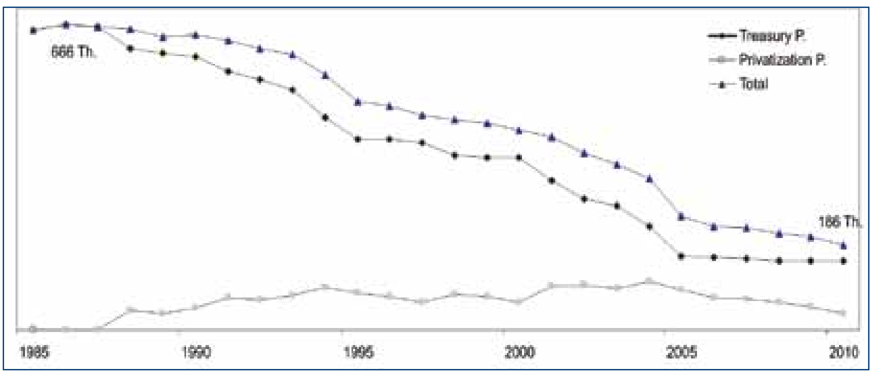
Figure 2 – Lower share of public investments



	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SOE/Total Public	29%	27%	29%	24%	20%	19%	9%	17%	14%	13%
SOE/GDP	1,2%	1,3%	1,0%	0,9%	0,8%	0,6%	0,3%	0,6%	0,5%	0,4%

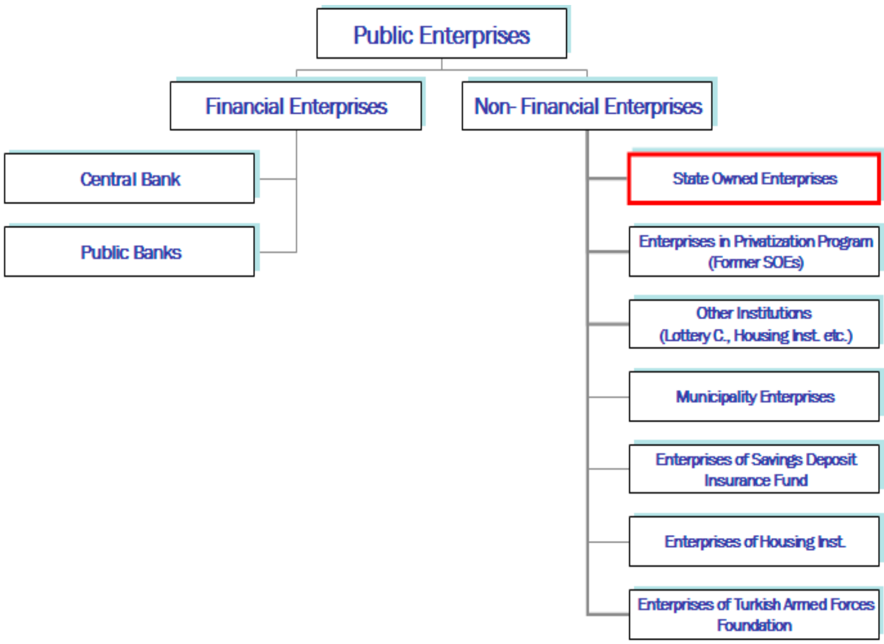
There is also a large drop in employment by SOEs during the last 26 years. The have downsized by 470,000 employees, which is 4% of the total employment in the Turkish economy, as illustrated in Figure 3.

Figure 3 – Lower levels of employment



Public enterprises are classified as shown in Figure 4. Public banks are classified as Financial Enterprises, and the remaining entities are classified under Non-financial Enterprises: SOEs, Enterprises in a Privatization Program, Local Administration Enterprises, etc.

Figure 4 – Classification of Public Enterprises



The ownership is represented by the Treasury of which it has 100% share (Privatisation Administration portfolio not accepted as a SOE). Members of the board are appointed by a joint decree (Line Minister, Prime Minister and President). The Treasury can get dividends or give capital injections to these enterprises. They are audited by the Turkish Court of Accounts and subject to inspection of certain issues by the Treasury and line ministry; approval of financial statements is the responsibility of the Grand National Assembly, and there is no external auditing of SOEs. Boards are composed of six members, one of whom is both chairman and CEO, and five of the members (including the chairman) are appointed upon the nomination of the line minister. Two of these five members must be selected from the deputy CEOs of the company upon the nomination of the line minister, and one member is appointed upon the nomination of the minister responsible from the Treasury.

3. Concluding Remarks and Future Prospects of PSEs sector

There are four documents that contain the future target for SOEs. One of them is the General Investment and Financing Program for SOEs, prepared by the Treasury and the Ministry of Development; it serves as a financial forecast of the next year for budgetary purposes. The next one is the Mid-Term Program for the General Government Sector, prepared for a 3-year period to estimate future risks and opportunities on the budget. Strategic Plans fall under the responsibility of each government agency and explicitly state the mission and vision of each SOE.

Responsibilities and limitations of SOE management are only provided generally. Each company is free to determine its prices, but the prices cannot be set below cost. This is only possible through intervention by the state for social purposes. In this case, the state covers the loss and an additional 10% compensation for forgone profits.

Employment policy is very rigid and employment costs are too high. There are plans for liberalisation of railway and postal sectors, although the energy sector has already been completely privatised.

Turkey's current plan is that the state should have a new role in the economy as a strong regulatory and supervisory body, but ultimately without its own production and trade activity. In addition, it seeks the adoption of corporate governance principles for public enterprises as well as the implementation of best practices. Its goal is to create a more autonomous managerial environment and a clear distinction between financial and policy objectives.

Managing State-Owned Enterprises – the UK Experience

Stephen Lovegrove[18]

During the 1980s and 1990s, the UK privatised many of its state owned companies. As a result, the number of businesses remaining in public ownership in the UK is comparatively low. There are four main themes arising from the UK experience which assist in identifying whether a state becomes a good shareholder or not:

Personnel

Not all civil servants have the correct skill sets or experience to deal effectively with corporate issues.

Solution: The UK Government has worked hard at bringing in talent from the private sector, and it has found it relatively easy to recruit specialist professionals from there. Often, the more intellectually complex environment in government is of great appeal to these specialists. Today, the Shareholder Executive constitutes some 30 civil servants from the public sector, complemented by a further 30 people from the private sector, and the transfer of these skills is an important part of our role.

Objectives

The biggest challenge today is to find a balance between meeting the public policy objectives of the SOEs while also addressing their inefficiencies, which in public companies are often very unclear. For example, the British broadcaster, Channel Four, is required by legislation to maximise its programming output rather than have any profit targets. In practice it attempts to make a small profit, which it keeps on its own balance sheet, every year. But this profit is an order of magnitude lower than that recorded by its commercial rivals. Although Channel 4 is well run, it is sometimes difficult to know where this foregone profit is spent – on programming or on inefficiencies.

Solution: There is no substitute for utmost clarity between commercial and public policy objectives. In the UK, the Shareholder Executive has to make sure that public policy objectives are debated and documented as clearly as possible, before seeking to achieve a degree of formal delegation for commercial matters, and sometimes contractual arrangement, with policymakers.

[18] Chief Executive, Shareholder Executive

Governance

Historically, the British Government has not been comfortable with an aggressive exercise of its rights and responsibilities as a shareholder. As a result, management and the boards of state-owned companies were on occasion able to manage the business as they saw fit with no real sense of accountability, hence one reason why the Shareholder Executive was established.

Solution: Without impinging on the legal and fiduciary duties of the boards that we appoint, the Shareholder Executive seeks to apply the highest standards of corporate governance to our companies. This includes: formal board member selection processes, regular Board Reviews, properly constituted Board Committees, and clear targets and expectations. To the extent possible we seek to insulate politicians and policy makers from these everyday corporate matters.

Capital

One of the important functions of the shareholder is to make decisions about and provide adequate capital to the company. This has been a difficult subject in the UK, where capital is scarce – particularly in current times. We have a strong and sympathetic ultimate shareholder in the UK Treasury, but the Treasury typically will be reluctant to provide additional capital given the many calls on its funds – one of the reasons that the Shareholder Executive sits within the Business department rather than Treasury itself.

Solution: There is no clear cut solution to this issue, other than acknowledging that the only stable source of financing comes from the private sector – further reinforcement to the UK's natural prejudice in favour of privatisation.

Can Government be a good owner?

Based on the UK's experience, it can, but there are formidable difficulties to be overcome in doing so. The techniques for becoming a good owner need to be mastered, as there is often no substitute for state ownership, especially where public policy issues are paramount. The UK experience, though, is that a more lasting solution to the issue regarding good ownership is to be found in the private sector, and we continue to push forward privatisation models where we can.

Enhancing Performance and Governance in State-Owned Utilities[*]

Dr. Maria Vagliasindi[19]

State-owned enterprises (SOEs) dominate the infrastructure sectors and play the almost exclusive role of providers of electricity, gas, water, and railways. Despite the several rounds of privatisation and private participation from 1990 to the present, a large proportion of utility services are still delivered by SOEs in the developed and developing regions of the world. Yet, limited research in the academic sphere on policy agenda focuses on the successes and failures of the public sector (Gómez-Ibáñez, 2007 and Vagliasindi, 2011a and 2011b).

SOEs face particular challenges from the adoption of standard governance rules that were designed for privately owned enterprises because of their often different and sometimes conflicting roles. Such roles include the government as a political actor, owner, policymaker and regulator of the infrastructure sectors. For example, the government as a representative of political constituencies may seek to set privileged terms for infrastructure services. Or it may care more about the achievement of equity objectives, such as ensuring universal access to services by charging tariffs below costs or extending service into unprofitable areas. The government may try to interfere in the management of the utility in ways that can translate into excess employment or rampant corruption. It may also seek below-cost or free access for politically powerful constituencies, potentially giving rise to capture.

Effective regulation of SOEs requires the clarification and separation of government roles and functions. Transparent policies and funding should help clarify the role of the government and limit political patronage. Government may consider clarifying its role and expectations as the owner of the utility through a shareholder contract and make SOEs subject to company law through the creation of a legal identity separate from the government, to follow provisions of financial autonomy, liability for tax and dividends, to pursue profitable strategies and to be insulated from political pressures. The need to adopt such solutions is also supported by theoretical models of corruption that arose from the self-seeking behavior of government officials (Shapiro and Willig, 1990; Shleifer and Vishny, 1994; Boycko et al., 1996).

It still remains to be seen whether standard governance channels (for instance regulation) can be effective as tools to enhance the performance of SOEs. This depends on whether the SOE regulator will be empowered to implement effective

* This note is based on previous work, including Vagliasindi (2011a and 2011b). I am grateful to Vijay Iyer and participants of the High Level Meeting of the State Ownership Authorities held in Ljubljana, Slovenia on 5-6 September 2011 for the helpful comments and suggestions. The content of this paper does not necessarily reflect the views and policies of the World Bank.

19 Lead Economist, Energy Anchor, Sustainable Energy Department, World Bank

economic regulation, free from political interference from the government as well as regulatory capture from the industry. It also hinges upon whether the regulator can influence reward systems inside the firms. In addition, public and private enterprises may respond in different ways to the same regulatory incentives, and some evidence from developing countries shows this to be the case (see Berg et al., 2005). Guasch and Straub (2005) also model the interaction between corruption and regulation but in the context of its effects on the renegotiation of infrastructure concessions in Latin America.

Analysis from a new database, including about 60 enterprises providing electricity, water and railway services in 15 developing countries, finds strong evidence of the lack of effectiveness of regulation in enhancing SOE performance (Vagliasindi, 2011b). There is some evidence of more promising channels, such as corporate governance changes and public listing.

Some of these options can only be used in special circumstances. Countries with a functioning capital market may want to consider listing (even a minority stake of) the infrastructure service provider on the stock exchange. Capital markets not only provide the needed capital for investment, but also facilitate better disclosure of information and monitoring of performance by shareholders. In many individual cases, capital market reforms through public listing proved to have a major impact on performance. For example, Sabesp (Brazil) and Manila Water (Philippines) in the water sector were both consistently able to improve their performance over time after being listed in the local stock exchange market. Even in less developed countries, results of corporatisation and public listing have been impressive. Kenya, for example, corporatised its electricity distribution firm and its generation firm, and then issued a minority of shares in each firm on the Nairobi Stock Exchange. The 2006 IPO of 30 percent of Ken Gen shares raised US $35 million. If public listing is not feasible, empowering the board to exercise effective monitoring of management may prove to be a formidable challenge for SOEs. More attention to board procedures, particularly related to the board selection and evaluation process, is essential. Ensuring sufficient continuity of services to directors is particularly crucial to improve corporate governance. In addition, other factors that may reduce directors' abilities to monitor corporate activities, such as their political connections, years in office, age profile, and the number of boards on which they sit, need to be handled more carefully (Vagliasindi, 2008).

How can a country make regulation of SOEs more effective in enhancing performance, and how might it assure that the regulatory framework translates into the firm's internal reward systems? Some innovative tools might be used. For example, the performance contract between the Government of Mozambique and Electricidade de Mozambique specifies financial and operational performance that the government expects the utility to achieve within a few year period. Mozambique attempts to use a regulator to publicly monitor the performance of state enterprises under a performance contract. Public monitoring entails the general Mozambican public to be informed of the results of the periodic evaluations of the utility's performance that are made by the regulator. However, there are no explicit rewards and penalties apart from the ability of the Government to replace the President and Executive Board of the utility.

References

Berg, S., Lin, C. and Tsaplin, V., 2005. "Regulation of State-Owned and Privatized Utilities: Ukraine Electricity Distribution Company Performance." Journal of Regulatory Economics 28 (3): 259–87.

Boycko, M., Shleifer, A. and Vishny, R. W., 1996. "A Theory of Privatisation," Economic Journal, 106 (435): 309–19

Gómez-Ibáñez, J. A., 2007. "Alternatives to Infrastructure Privatisation Revisited: Public Enterprise Reform from the 1960s to the 1980s." Policy Research Working Paper No. 4391, World Bank, Washington, DC.

Guasch, J. L. and Straub, S., 2005. "Infrastructure Concessions in Latin America: Government-led Renegotiations." Policy Research Working Paper Series No. 3749, World Bank, Washington, DC.

Shapiro, C. and Willig, R., 1990. "Economic rationales for the scope of privatisation" in: Suleiman, E.N. and J Waterbury, eds., 1990. The political economy of public sector reform and privatisation, (Boulder: Westview Press).

Shleifer, A. and Vishny, R., 1994. "Politicians and firms", Quarterly Journal of Economics 109: 995–1025.

Vagliasindi, M., 2008., "The Effectiveness of Boards of Directors of State Owned Enterprises in Developing Countries", Policy Research Working Paper No. 4579, World Bank, Washington, DC.

Vagliasindi, M., 2011a "How to Improve the Performance of State Owned Service Providers", mimeo, World Bank, Washington, DC.

Vagliasindi, M., 2011b "Public versus Private Governance and Performance: Evidence from Public Utility Service Provision", International Handbook of the Economics of Corruption II, Edward Edgar (ed.) 185–206.

Final Notes coordinated by Dr. Peter Kraljič[20]

The participants at the High Level Meeting of the State Ownership Authorities "State as an owner - ownership policy, execution of state interests and fostering of public-private dialogue" organized in Ljubljana on September 5–6, 2011, brought into discussion a number of issues to be taken into account with regard to public sector enterprises. In spite of the sometimes diverging opinions, several converging points can be identified. Thus the participants have generally agreed that one of the crucial preconditions for successful PSE governance is to clearly define the strategic goals the states wish to achieve with the help of their PSEs.

Countries aiming at becoming true market economies should continue the privatisation process as Michael Offer (Germany) argued, and one of the main aspects related to privatisation is the institutional framework as well as clear aims and objectives with regard to the privatisation process.

Another subject which was raised was the question of centralisation versus decentralisation, thus if the state wants to achieve some non-economic goals, perhaps the management of companies following non-economic goals should be left to the ministries such as energy, infrastructure, telecommunications, etc., whereas if the state wants to follow strictly economic orientations, e.g. improving the budget, etc., the PSEs' management should be more centralised as Samo Kutoš (Slovenia) emphasized. Similarly Murilo Barella (Brazil) stressed the PSEs' role in development. If the PSEs are seen as instruments of economic development, probably the best solution is to have them administered by ministries, though economically this is not profitable.

Ivo Habets (the Netherlands) expressed the idea that the level playing field between private and public companies is one of the key factors which should be considered; in his view the equality of the state as shareholder and the private shareholders is absolutely necessary. Moreover, the question of the level playing field is an issue to be considered in the future, particularly given the economic zones we move in might have some different regulations, and the way in which these regulations are set to achieve a common global standard according to the High Level Meeting rapporteur, Peter Kraljič.

Erdal Trhulj (Bosnia) stressed that there is no precise formula for the success of state owned enterprises. Thus, a successful model in one country does not automatically mean that it is applicable in another country. Also, a successful example in a particular country does not mean that it can be applied to another public enterprise in the same country.

[20] Director Emeritus of the McKinsey & Co. Inc.

Public enterprises should be approached in the same way as private companies: a clear plan that targets good management is crucial for their performance as expressed by Erdal Trhulj (Bosnia). Besides advantages, PSEs also have certain disadvantages – one of the main disadvantages being related to the issue of property. For instance in ex-Yugoslav countries the prevailing idea is that if an enterprise belongs to the state, it either belongs to no one or it belongs to everyone, and this is the reason why many PSEs are not profitable.

There is also no universal recipe for each country in so far as the public and private sectors are concerned. Though lessons are learnt from different international experiences, one should also concentrate on the local conditions and historical development of a particular country. Dmitry Kolkin (Belarus) pointed out that one solution is that governments should determine some sectors in which they will participate while the rest should belong as private property to the private sector.

The risk that there are too many rules, and that the PSE environment becomes a very rigid, rule-driven environment always exists. On the one hand, states have important values while on the other, there is performance to consider – and there is always a trade-off between the two. Concerning standards, Hadil da Rocha Vianna (Brazil) suggested that the standards and models offered by the OECD are extremely important to European countries, but there might be other existing models and these other models should also be tested, applied and verified.

As mentioned above, there are various ways in which different states govern public enterprises; however, there are always examples of best practices. At the end of the High Level Meeting of the State Ownership Authorities in Ljubljana, Peter Kraljič summarized the conclusions and offered some future prospects for the state enterprises. We are faced with very complex environments and these environments are displayed along several levels:

- The giga level (global) – There are no rules and there are many companies or countries exploiting the global game in very different ways.
- The big economic zones, for instance the European communities, NAFTA, Mercosur, Asian or African zones – This is a mega level, and these mega levels are not fully coordinated; sometimes they cooperate and sometimes they do not.
- The macro level (the state) – States remain very important because they play a decisive role in the developments within each individual country. But no matter the form or combination, one role is always constraint. The amount of autonomy a state still enjoys and how this autonomy is best exploited in the benefit of the people is still the ultimate objective.
- Economic sectors – The questions which arise are which economic sectors exist and how competitive are they (industrial, non-industrial, the service sector, a large variety from country to country, etc.)? And which ones are vital for a certain country? Why?

- The micro-level (the companies within a particular sector) – How do you optimize the performance of an individual company?
- The nano-level (the individuals, people or richness of a country) – What is the best way to utilise people, especially in countries which have no natural resources?

Peter Kraljič summed up a series of questions and challenges the PSE sector faces:

- State-owned companies are very important in many environments; they are still a very vital driver of future economic progress and the progress of the society. The basic issue is to determine the right trade-off between society's or the country's goals versus market imperatives.
- Appointing the PSE boards, including their selection, remuneration and monitoring processes – There is the trap of having too many political appointments instead of competence driven appointment;
- Privatisation – identifying the strategic sectors and the criteria for a certain sector to qualify as strategic, the forms of privatisation (tenders, auctions), how much to privatise (big versus small scale privatisation) and the rate of privatisation (how fast can one go), defining the national interest
- Competitiveness as an important dimension – there is an evolution of consolidation and higher performance, and maybe even PSE competitiveness, at the international level.
- The institutional framework defined by governments or other institutions (for instance the OECD)
- PSE efficiency, accountability, transparency and talent – Do we have the talent, do we have the right people in these state-owned enterprises? How do we remunerate them? How do we motivate them?
- The right proportion of state and private companies and the right level of involvement of the owner, i.e. the right depth of state involvement at a certain stage of development
- Cultural change, performance culture and performance ethics
- Absolute commitment of the governments in the sense of urgency and aspiration
- Trade unions as important accelerators or barriers – Particularly in countries in which everything used to be state-owned, there might be resistance to privatisation.
- Foreign direct investments – How do we to achieve them and where do we want them?
- The state must be a good and responsible owner, and it is crucial to know how to establish this ethic of responsible ownership in state-owned enterprises.

Last but not least the ICPE Director General, Štefan Bogdan Šalej, in the closing speech touched upon the fact that the strict financial results should always be supported by the social aspect and by human rights.

An Experience through Disinvestment in India

Gupta Seema [21], P.K.Jain [22], Surendra S. Yadav [23] and Sushil[24]

INTRODUCTION

The emergence of disinvestment was recognized in the 1990s when the Indian economy was continuously facing a high burden of financial debt (nationally and internationally). Due to its financial burden constantly increasing since the 1980s, the economy was on the verge of financial disaster. Disinvestment was conceived as an important measure to salvage such a grim situation; evidently, it had deeper implications than simply selling government equity at the best price. It was expected to contribute towards the growth of the Indian economy by promoting competition that, in turn, would lead to cost reduction, improved quality and operational efficiency. Likewise, disinvestment was also expected to attract global capital as well as domestic capital. Above all, disinvestment of government equity in PSEs has many social, economic and political implications (Ray and Maharana, 2002).

The objective of this paper is to assess the financial performance of the disinvested central public sector enterprises (PSEs), primarily in terms of profitability and operating efficiency. For better exposition, the paper has been divided into seven sections. An overview of the disinvestment process in India has been presented in section one. Section two deals with a glimpse into the literature review. Section three provides a conceptual framework in terms of scope, methodology and sources of the data. The impact of disinvestment has been examined under section four. Section five measures the impact of the degree of disinvestment on the financial performance of disinvested PSEs. An analysis on the basis of the size of assets has been carried out under section six. Lastly, the concluding observations have been enumerated in section seven.

SECTION I
AN OVERVIEW OF DISINVESTMENT

The objective of this section is to provide a brief account of the rationale for the disinvestment made in PSEs and the major events leading to the process of the disinvestment policy.

Genesis and Rationale

The constant increase of the financial and economic burden faced by the government

[21] Research Scholar, Department of Management Studies, IIT Delhi
[22] Professor of Finance, Department of Management Studies, IIT Delhi.
[23] Professor of Finance, Department of Management Studies, IIT Delhi.
[24] Professor of Strategy, Department of Management Studies, IIT Delhi.

of India during the 1990s forced the government to incorporate disinvestment as an important element of reforms. The increased revenue expenditure of the government on items such as interest payments, wages and salaries of the government employees and subsidies left the government with hardly any surplus for capital expenditure on social and physical infrastructure. While the government would like to spend on basic education, primary health and family welfare, large amounts of resources were blocked in several non-strategic sectors such as hotels, trading companies, consultancy companies, textile companies, chemical and pharmaceutical companies, consumer goods companies, etc. All these factors made disinvestment of the government stake in the PSEs absolutely imperative.

Disinvestment Policies and Process

The proceedings of disinvestment started with the Budget 1991-92, outlining a disinvestment of 20 percent of government equity in select PSEs in favour of investors, mutual funds and workers. The Rangarajan Committee Report, April, 1993 emphasized the need for substantial disinvestment. The report stated that the percentage of equity to be divested for the strategic public sector should not be more than 49 percent. All other PSEs were to be considered as non-strategic, where the government stake could be reduced to 26 percent.

A decision pertaining to the percentage of disinvestment would depend on two factors: first, whether the industrial sector required the presence of the public sector as a countervailing force to prevent the concentration of power in private hands and second, whether the industrial sector required a regulatory mechanism to protect consumer interests in the face of privatization. However, the government did not take any decision on the recommendations of the Rangrajan Committee.

During the initial period, the government continued to disinvest three to five percent of the equity in different non-strategic PSEs every year. This incremental disinvestment, or more popularly, the minority privatization was more governed by the compulsion of financing the fiscal deficit of the government (ICFAI, August 2000). This provided stronger commercial considerations in response to normal shareholders' expectations.

Pursuant to the policies of the United Front government, a Disinvestment Commission was set up in 1996. The Disinvestment Commission, by August, 1999 had made specific recommendations on 58 PSEs; it suggested a shift from public offerings to strategic/trade sales through transfers of management instead of public offerings, in accordance with the recommendations of the Rangarajan Committee in 1993. As of December, 1999, the government had created a separate Department of Disinvestment to actively pursue disinvestment.

Furthermore, with the Budget 1999-2000, the government continued strengthening the strategic units and privatizing non-strategic ones through gradual disinvestment or strategic sale, and devising rehabilitation strategies for weak units. An important highlight of the policy was that the expression ‘privatization’ was used for the first time.

During the period 1991-2000, the sale of minority shares of public sector undertakings had generated resources of Rs. 19,000 crore (Rs. 190,000 million). Most of the shares during this period were picked up by financial institutions.

Budget 2000-01 highlighted for the first time that the government was prepared to reduce its stake in the non-strategic PSEs below 26 percent if necessary; it also stated that there would be increasing emphasis on strategic sales, and the entire proceeds from disinvestment would be deployed into the social sector, organizational restructuring, and the closing of PSEs which could not be revived, etc. As the term of the first Disinvestment Commission expired in 1999, a new Disinvestment Commission was constituted in July 2001, under the chairmanship of Dr. R. H. Patil, to advise the government on disinvestment in those public sector units which were referred to it by the government. The Disinvestment Commission had given its recommendations on 41 PSEs, including review reports on 4 PSEs already studied by the earlier Commission, and from which 20 reports had been submitted in the year 2003-04.

The Ministry of Disinvestment was converted into a Department under the Ministry of Finance, effective 27 May 2004, and was assigned all the work relating to disinvestment which had been handled by the Ministry of Disinvestment. The disinvestment of government equity in PSEs is required to be carried out in accordance with the policy laid down in the National Common Minimum Programme (NCMP).

On 27 January 2005, the government decided to constitute a ‘Fund’ into which the realisation from the sale of minority shareholdings of the government in profitable PSEs would be channelled, namely to the National Investment Fund. The Fund would be maintained outside the Consolidated Fund of India and would be professionally managed by selected public sector financial entities, which have the requisite experience to provide sustainable returns to the government without affecting the corpus.

During the year 2004-05, the government realised a sum of Rs. 2,765 crore (Rs. 27,650 million), out of which the major receipt of Rs. 2,684 crore (Rs. 26,840 million) was from the sale of 43.29 crore (432.9 million) equity shares of Rs. 10 each of the National Thermal Power Corporation Ltd. (NTPC) out of the government of India holding. A sum of Rs. 64.81 crore (Rs. 648.1 million) was realised from the sale of shares to employees of Indian Petro Chemical Corporation Ltd. (IPCL). Further, no target was set by the government during the period from 2005-06 to 2009-10, although the government did realise Rs. 1,569.68 crore (Rs. 15,696.8 million) from the sale of Maruti Udyog Ltd. shares to their employees and to the Indian public sector financial institutions and banks. No disinvestment took place during the period from 2006-07 and 2008-09. In 2007-08, the government realised Rs. 4,181.39 crore (Rs. 41,813.9 million) from the sale of equity shares of Maruti Udyog

Ltd. (MUL, Rs. 2,366.94 crore/Rs. 23,669.4 million), Power Grid Corporation of India Ltd. (PGCIL, Rs. 994.82 crore/Rs. 9,948.2 million) and Rural Electrification Corporation Ltd. (REC, Rs. 819.63 crore/Rs. 8,196.3 million) through the sales of residual shareholdings and minority shareholdings. However, the receipts through the sale of minority shareholdings in NHPC (Rs. 2,012.85 crore/Rs. 20,128.5 million) and Oil India Ltd. (OIL, Rs. 2,247.05 crore/Rs. 22,470.5 million) during 2009-10, the government realised Rs. 4,259.90 crore (Rs. 42,599.0 million).

The proceeds from disinvestment and related transactions from April 1991 to March 2010 amounted to Rs. 57, 682.93 crore (Rs. 576,829.30 million). At present (March 2010), 45 central PSEs are listed on the stock exchanges.

The government used various modalities of disinvestment ranging from bundling and bidding, then followed by tendering and global depository receipts for disinvestment. It is being suggested that in the profitable enterprises equity should be offered to the public and also to the employees. It is expected to accord better acceptability; it also provides opportunity to people in sharing wealth through the well-established disinvestment process. The strategic sale route is beneficial, as concentrated ownership offers incentive to maximize long-term enterprise profits through good governance. Disinvestment is expected to result in greater resources for the government, a lesser debt burden, a healthier fiscal position and a vibrant economy.

SECTION II
LITERATURE REVIEW

To gain better insight, literature relating to privatization or disinvestment has been further subdivided into two parts: specifying global experience and focusing on the Indian perspective.

Part I – Global Perspective

Kay and Thompson (1986) examined the privatization in U.K. and the sale of government industrial assets. The government sees the denationalization of public industry serving a multiplicity of objectives. One aim is to improve the economic performance of the industries concerned. Another is to resolve the persistent problems of management and control, i.e. the relations between government and nationalized industries. The treasury is greatly interested in the revenue which can be obtained from privatization. Although the objective is rarely articulated, privatization may also be seen by the government as a means of disciplining the power of public sector trades unions. A final objective is the promotion of a kind of popular capitalism through wider share ownership.

Little (1952) was concerned with PSEs' neglect of appropriate incentives for productive efficiency. His emphasis was on the burgeoning literature on business management, which would stress increasingly that efficient organization required managers who would have specific objectives and have their performance monitored in relation to them.

Bishop and Kay (1989) compared the performance of privatized UK companies with those that stayed in the public sector. They found no strong evidence to indicate that privatized firms perform better. They measured profitability in terms of return on capital employed (ROCE) and return on sales (ROS), and found both ROCE and ROS were generally higher among the privatized companies than among the public sector ones, but this had been true of those companies even before they were privatized. Thus, it appears that the more profitable firms were sold early, leaving the less profitable ones in the public sector.

Hammer et al. (1989) examined the management dimension before the state-owned enterprises (SOE) were privatized. The authors suggest that privatization strategy is closely linked with overall business strategy. It is to ensure the opportunities afforded by the operation which provides long- term profit enhancement. Findings suggest that privatization increases the complexity of the business problems. It effectively changes the environment and thus increases the demands placed on management in improving long-term profitability. The privatization strategy must provide a clear step by step process for achieving the state's goals, the new direction of the company, implementing vision and identifying and attracting a suitable group of investors. The privatization strategy has to be closely linked with the overall business strategy in order to exploit the long-term profit enhancement opportunities.

Lorch (1991) compared the performance of 24 privatized textile mills in Bangladesh with 35 other mills that the government did not privatize by using unconventional measures of performance. He focused on four functional areas: procurement, production, sales and the support function. 'Efficiency' was defined as 'cost-advantage'. He concluded that the Bangladesh textile industry does not offer a very strong endorsement of privatization as far as its efficiency implications are concerned.

Megginson et al. (1994) compared the pre and post-privatization financial and operating performance of the period three years after privatization with that of three-years-before for 61 companies from 18 countries (6 developing and 12 industrialized) and 32 different industries that experienced full or partial privatization during the period from 1961 to 1989. Under these companies the government sold off its equity, but no capital flowed to the firm itself. Therefore, any improvement in performance after disinvestment must be traced to changes in incentives, regulation and ownership structure rather than to cash injections into the firm from a new capital issue. They documented significant increases in profitability, output per employee, capital spending and total employment after privatization.

Martin and Parker (1995) examined whether 11 British firms privatized from 1981 to 1988 had improved their profitability (measured as return on invested capital) and efficiency (annual growth in value added per employee-hour) after being disinvested. They found mixed results.

Ramamurti (1997) examined the restructuring and privatization of Ferrocarilla Argentinos, the Argentine national freight and passenger railway system. He observed the incredible 370 percent improvement in labour productivity and an equally striking 78.7 percent decline in employment (from 92,000 to 18,682 workers). He stressed that performance improvement could not have been achieved without privatization.

Sueyoshi (1998) examined the economic assertion by comparing Nippon Telegraph and Telephone (NTT), a Japanese government company's performance before and after its privatization and presented the management problems occurring within the partial privatization.

This empirical study found that NTT's partial privatization had an impact on its productivity enhancement, primarily due to a natural reduction in personnel. The company failed to achieve any significant improvement in cost management even after its privatization. The performance and corporate behaviour of a firm cannot be determined only by its ownership. The two performance measures are influenced by many other external factors, including the type of corporate environment (regulation or deregulation) and the type of client (government or private firms). A public firm facing serious competition may behave as a private firm. Meanwhile, as identified in this case study of NTT, a private firm under governmental regulation may still function like a public firm.

Boubakri and Cosset (1998) examined the change in the financial and operating performance of 79 companies from 21 developing countries that experienced full or partial privatization during the period from 1980 to 1992. The authors used accounting performance measures adjusted for market effects in addition to unadjusted accounting performance measures. Both unadjusted and market-adjusted results show significant increases in profitability, operating efficiency, capital investment spending, output, employment level and dividends. They also found a decrease in leverage following privatization but this change is significant only for unadjusted leverage ratios. It is generally less significant when performance ratios are adjusted for market effects; further, they examined how privatization in developing countries affects the financial and operating performance of their public enterprises.

Bradbury (1999) carried out a case study of the comparative financial performance of Government Computing Services (GCS) as it moved from a government department into privatization. The results show that the financial performance of GCS improves. The prime performance measures used in the study are return on equity (ROE), return on assets (ROA) and return on revenue (ROR). Growth in revenue is also measured. Similar measures are employed in major studies that utilize accounting ratios to examine economic performance (Rumelt, 1974; Boardman and Vining, 1989; Karpoff and Rice, 1989).

Gupta et al. (2000) stated that fiscal constraints seem to be the main motivating factor in choosing partial privatization, and this is consistent with the empirical findings. It is also possible, however, to interpret revenue maximization as a political objective. The ability to generate revenue enables a government to soften the employment impact of the transition process; it raises the government's ability to pay state workers and so on. These factors are arguably very important in gaining support for the transition process.

Abelson (2003) reported nine cases that covered a variety of Australian jurisdictions, industry and disinvestment methods. Out of the nine case studies, the author derived three main lessons. First, long-term financial returns have played very little part in the decision to privatize. In all cases, it appears that citizens of Australia were not adequately compensated for the loss of previously collectively owned assets and governments are concerned mainly with short-term issues. Second, considerable transformation had taken place in many of the organizations in the preparation for the sale, including assistance for the government; he argued that this transformation and assistance were largely responsible for the success of the organizations post-sale. Organizational transformations would have occurred in the absence of the privatization. Third, the author reports that there is a consistent pattern of winners and losers from the privatization. The winners were the financial institutions, the new shareholders and private consultants; the main losers were future taxpayers and the workers in the pre-sale organizations.

Hamid and Chao (2006) used a simple model to identify the conditions for assessing the privatization effect on the environment. This paper showed that privatization can have a negative effect on the environment.

Yip et al. (2009) examined the issues of determining long-term (sustained) superior financial performance. They used the frontier analysis technique to identify relative performance and addressed the three critical issues in the measurement of performance, i.e. balancing short-term and long-term performance, capturing the multidimensional nature of performance, and finding the right peer comparisons. The approach provides managers and analysts a powerful logical heuristic that can help them in making quicker and better decisions, given the failure of past performance to signal how firms would be able to weather a pervasive global crisis.

Part II - Indian Perspective

Jain (1989) used an incremental analysis to assess the performance of a Development Bank at that time, the Industrial Finance Corporation of India (IFCI) on the basis of financial function and development function criteria. The financial function measures the operational efficiency in terms of profitability of its investment operations and a developmental function evaluates its allocational efficiency. The profitability has been analyzed in terms of operating earnings, cost of operations, gross and net margins on the loan portfolio and rate of return (ROR). The ROR was computed in terms of return on total assets (ROTA) and return on capital employed (ROCE) and both registered a marginal increase. The adequacy of ROR was judged by comparing actual ROR with expected ROR; actual ROR values were lower than the expected ROR, virtually during the entire time period of the study, and suffered financial losses. IFCI investment policy in financing new companies and industrial projects located in backward areas (as a part of its deliberate policy to achieve the objective of balanced regional development) was the probable reason of low profitability and depressed rates of return; it faced the challenge between developmental functions and economic functions in achieving profitability.

Kumar (1992) categorized SOEs on the basis of being high or low with reference to market structure, efficiency and social obligations. The model suggests divestiture of enterprises which are low in efficiency and social obligations. A SOE set up as a statutory corporation under an Act of Parliament or as government department first needs to be transformed into a stock corporation, subject to ordinary company laws so that shares can be offered to the private sector.

Basu (1994) conducted a study on the privatization of the developing country's agenda, which include restructuring, reform, commercialization, management-cum-technology contracts and leasing. For this purpose, prior to divestiture, the processes included joint venture, hire purchase and disinvestment of minority/majority/full shareholding through public offer or private sale. The study supports the policy of state government that selective privatization /disinvestment of loss-incurring public and cooperative enterprises operating in 'non-core' sectors. The primary objective of the government's privatization policy was to revive potentially viable loss-incurring enterprises and to safeguard the interest of the workers and to create opportunities for further job creation by catalyzing the dynamism of the private enterprises. Efforts were made to establish a system of good corporate governance practices in these core enterprises, so as to enhance transparency and accountability in their operations and stimulate their performance.

Gouri (1997) observed that privatization in India is low. Privatization for ownership transfer is limited to disinvestment of PSEs for raising non-inflationary resources. At the same time, there is a gradual withdrawal of budgetary support from PSEs resulting in a gradual dilution of equity as enterprises tap the capital market. Simultaneously, economic liberalization policies have emphasized a level-playing field for the public sector. In terms of economic management, and more so, public sector management, there is lack of a comprehensive policy on privatization that can result in unexpected outcomes which may not be all that expedient.

Singh (2004) suggested that the resources of state-owned enterprises (SOEs) are used not only to generate employment and provide facilities for certain sections of society, but also to sell the products at lower prices than the cost incurred. This was triggered by organizational efforts towards non-economic activities which led to economic inefficiency and failure.

Naib (2004) stated that disinvestment of equity was the key determinant of the Indian public sector reforms. The common perception amongst various countries that engaged in a substantial programme of divestiture is that this not only raises resources for the governments and reduces fiscal deficit but also releases resources for public investment in essential areas like primary education and basic health. It is accordingly argued that such programs ultimately are desirable to create jobs and contribute to mass welfare in the long-run. It has been revealed that the vast investments failed to produce the surpluses which they were expected to generate, and the return on capital employed was quite low. This raised the issue of whether the present ills of the SOEs can be corrected by a change in their ownership.

Disinvestment Manual (2007) contains no standard recipe for disinvestment in PSEs at the national level or at the state level. It suggests that the country would do well to learn from the successful experiences of the West; it would have to be careful with the pitfalls which were responsible for setbacks to some of the economies in the East.

In the final analysis, while experiences of other countries are available to India by way of guidance, India would have to evolve its own techniques, best suited to its level of development. The historic, cultural and institutional context influences the way in which and the pace at which privatization is implemented. Where a market economy is not fully developed, ways would have to be found to safeguard the interests of consumers and investors which would ensure a fuller play to the wealth creating role of the entrepreneurs.

Kaur and Singh (2005) addressed the utility and process of disinvestment in India which leads to cost reduction, improved quality and operational efficiency. It improves efficiency and pushes up growth rates; growth provides jobs and employment; disinvestments also help to attract global capital as well as domestic capital. They highlighted the two main causes of its failure, i.e. the significant burden of non-commercial obligations of the state and untrammelled discretionary power with the government that erodes its autonomy. They caution that disinvestment does not mean that there is a move to withdraw investment; rather it is the channelling of the investment in a more productive and efficient way, so that it can prove itself as an acceleration of growth.

Gupta (2005) observed that partial privatization has a positive impact on profitability, productivity and investment. The study is based on 339 manufacturing and service sector firms owned by the central (247) and state governments (92) of India for the period 1990–2002. Firms experience a significant increase in profitability, labor productivity, R&D investment and intensity, asset size and employment after partial privatization. Partial privatization leads to an increase in the productivity of labour and output without layoffs.

Keswani and Shackleton (2006) demonstrated how a project's option value increases with incremental levels of investment and disinvestment flexibility. They emphasized that the option to disinvest is as important as the option to invest in enhancing project value.

Vadlamannati (2007) said that India is one of the fast-emerging economies in the world which is striving hard to control all its deficits while implementing all possible measures in the form of economic reforms, which were initiated in the 1990s. They attempted to answer whether privatization is one of the determinants of deficits. The empirical results show that the correlation of disinvestment and privatization (in India) in relation to these variables is very feeble and weak in view of the very small sized and slow-paced disinvestment and privatization program.

Arnold et al. (2008) suggested that conventional explanations for the post-1991 growth of India's manufacturing sector have focused on goods, trade liberalization and industrial de-licensing. However, the pace of policy reform has varied across sectors, and it is determined primarily by political considerations (Hoekman et. al., 2007). Sectors in which privatization and competition would mean restructuring and large scale lay-offs were slower to benefit from the reforms than those in which incumbents could remain profitable and employment would not decline even as foreign and local private competitors entered the market.

Notwithstanding the above notable works/studies on the subject, there has been no single study which examines in depth the impact of disinvestment on all major parameters of financial performance (profitability, liquidity, solvency, efficiency, productivity, etc.) of PSEs in India for the time span of nearly two decades. The present paper is a modest attempt to fill this gap.

SECTION III
SCOPE AND METHODOLOGY

The scope of the study is limited to non-financial central PSEs in India that pursued disinvestment. The sample consists of 38 disinvested PSEs (out of a total of 43 totally disinvested enterprises as at March 2007). The disinvested PSEs consist of central PSEs where less than 50 percent of the disinvestment was undertaken up to the year 2001-02. The sample is representative in nature, as it adequately represents all the industrial groups (pursuing disinvestment as per the Public Enterprises Survey). The enterprise performance before and after five years of disinvestment has been compared over a time span of 20 years (1986-87 to 2006-07) on a rolling basis; this is to ascertain whether there has been any significant change in financial performance due to disinvestment.

For this purpose, these phases have been divided on the basis of the last year of disinvestment, cut-off year being 2001-02. There are two major reasons for choosing the cut-off year as 2001-02. The first is that a small amount of disinvestment took place during the initial years in many of the PSEs. Due to several reforms and policies, the amount of disinvestment has witnessed a decisive increase in the succeeding years in certain PSEs; in operational terms, the cumulative amount of disinvestment (till the cut off year) turned out to be reliable. The second equally important reason is that the last year used for the purpose of the analysis in the study is 2006-07; to assess the performance of disinvestment, the five-year time-lag requirement gets fulfilled at 2001-02. For statistical tests, the first phase (five years prior to disinvestment) and the second phase (five years subsequent to disinvestment) are considered as two independent samples.

Relevant data (secondary) was collected from the various volumes of the Public Enterprises Survey. Financial performance was measured on the basis of aggregative and dis-aggregative analyses. In each analysis we relied primarily on 19 financial ratios pertaining to profitability, operating efficiency, leverage, liquidity and productivity. It may be recalled that the primary objective of disinvestment has been to enhance operational efficiency leading to better/higher profitability. Therefore, profitability and efficiency ratios are relatively of higher significance than liquidity and solvency ratios. This would constitute the focus while interpreting the results of the post-disinvestment *vis-à-vis* pre-disinvestment periods. Although, the computation of select financial ratios in each sample PSE was determined on the basis of the last year of disinvestment, and performance was measured five years before and five years after the last year of disinvestment, by considering the last year in that organization as the zero year, the summation of all the individual enterprises was further processed for descriptive and positional value analysis on a rolling basis.

Statistical tests, namely the t-test and 'analysis of variance' were used to assess the financial performance of disinvested public enterprises within a group of firms and with the group of firms during the second phase compared to the first phase. The entire set of data was analyzed with the Statistical Package for Social Sciences (SPSS).

To study the trend and its implications, the descriptive statistics and positional values, i.e. mean, median and quartiles were computed for each PSE. In addition, to overcome the variations of the sample data, mean of mean, median of median and quartile of quartile were also computed for each enterprise in each phase. To do away with the influence of extreme values, they were excluded from the data; the details of excluded values have been mentioned in the footnotes of the tables.

We relied primarily on the 19 financial ratios (related to profitability, operating efficiency, leverage, liquidity and productivity) to analyze the financial performance of the sample enterprises. Profitability was measured in terms of rate of return on investment and sales. For the purpose of analysis, the return on investment was computed in three ways, *viz.*, return on total assets (ROTA), return on capital employed (ROCE) and return on net worth (RONW). The first two rates of return highlight how efficiently financial resources are deployed by the PSEs and RONW indicates the return provided to the equity-owners (primarily government in the context of PSEs). ROTA was determined on the basis of earnings before interest and taxes (EBIT); it expresses the relationship between total income earned before interest and taxes and average total assets in use. Total assets in use includes the net block of fixed assets, other items in the nature of fixed assets, investments, total current assets and deferred revenue/preliminary expenditure, and it excludes accumulated deficits, capital work-in-progress and unallocated expenditures during construction, since these assets have yet to contribute to the services provided or revenue generated by PSEs. Investment refers to the amount of share capital or long-term loans invested by a holding company in its subsidiaries or *vice-versa* (Government of India, 2002-03). *Prima facie*, investments as well as income earned on such investments should have been excluded as they are made outside the business firms, but included them due to non-availability of data on interest/dividend income earned from such investments. Therefore, income derived from such investments form part of operating profit while computing ROTA.

ROCE indicates how efficiently the long-term funds of the lenders and owners are being used; it is a ratio of operating profit (EBIT minus other income or miscellaneous receipts) and average capital employed (includes the gross block of fixed assets less accumulated depreciation plus net working capital). ROTA and ROCE preclude the effect of financial structure and taxes, since government as an owner also gets the taxes. As a result, these ratios focus directly on operating efficiency. Furthermore, while ROTA is useful as an overall measure of performance in respect to operating efficiency, ROCE shows how efficiently the funds of owners and lenders are used (Jain and Yadav, 2005). In general, the higher the ratio the more efficient is the use of funds.

As far as RONW is concerned, it was computed by dividing net-profit after taxes minus preference by the average net-worth (share capital plus reserves minus accumulated deficit and deferred expenditures). It is important to note that the ROCE and RONW were not computed in the case of PSEs having negative net worth and negative capital employed. The reason is that the ratio provides ridiculous results when the denominator is negative. However, the numerator can be negative, as it indicates that the PSE has suffered a loss (at the computed negative rate) on capital employed/net worth. Therefore, positive net-worth and positive capital employed with negative net-profit and negative EBIT were included in the study; they signify that net-worth or capital employed is lying with the company but has earned negative profits or losses.

Secondly, return on the basis of sales was computed on the basis of operating profit margin (OPM) and net profit margin (NPM). The OPM represents the operating profit before any compensation was paid to the debt-holders. The ratio provides a clear view of profit margin (undistorted by financing patterns and tax calculations) referred to as earnings before interest and tax (EBIT) relating to sales. The NPM determines the relationship of reported net-profit after taxes to sales; it indicates the management's ability to carry on the business profitably and expresses the overall cost/price effectiveness (Helfert, 2003). Thus, the methodology outlined above is appropriate for evaluating profitability.

Similarly, efficiency or effectiveness in utilization of resources was determined on the basis of three dimensions. The first one is concerned with the efficiency with which assets are used in business enterprises by the management. Turnover is the primary mode for measuring the extent of efficient use of assets by relating them to net sales; they are total assets turnover ratio (TATR), fixed assets turnover ratio (FATR) and current assets turnover ratio (CATR). Low turnover is indicative of under-utilization of available resources and the presence of idle capacity. TATR indicates the efficiency with which firm uses its assets to generate sales. Generally, the higher the firm's TATR the more efficiently the assets are being used (Gitman, 2009). TATR, FATR and CATR are computed by dividing average net sales with average total assets in use, average fixed assets (excluding depreciation) and average current assets, respectively. Net sales exclude excise duty, commission, rebates and discount from gross sales. Total assets in use was determined by deducting the accumulated deficit, work-in-progress and unallocated expenditures during construction from the total assets (assets not in use merits exclusion); fixed assets include gross fixed assets minus accumulated depreciation plus other items in the nature of assets. It should be borne in mind that the current assets take into account five items, namely, cash and bank balances, sundry debtors, inventories, loans and advances and the stock of other current assets.

The second dimension of efficiency is based on examining the change in the holding period (in number of days) of various types of inventories and the collection period of debtors which are the sub-constituents of current assets. The objective of inventory management is to minimize the investment in the inventory and to meet the demand of products through efficient production and sales operations with a view to reduce carrying cost and stock-out cost. Inventory consists of raw materials, spare parts and other stores as the raw-material inventory holding period (RMIHP), work-in-progress inventory holding period (WIPIHP) and finished-goods inventory holding period (FGIHP). RMIHP is the ratio of raw materials consumed during the year and average raw materials at the beginning and end of the year; WIPIHP was computed on the basis of cost of production (represents all costs incurred in production/operation including depreciation but excluding excise duty) and average work-in-progress in the beginning and end of the year; it is to preclude the impact of changes in the excise rates from the analysis. Similarly, FGIHP is based on the relationship between cost of goods sold, i.e. cost of production plus opening stock of finished goods minus closing stock of finished goods (numerator) and average finished goods (denominator).

Debtor collection period (DCP) presents the relationship between gross sales (numerator) and average debtors in the beginning as well as in the end of the year (denominator). Debtors/receivables represent an important component of current assets among all the business corporate enterprises. It is an extension of credit that involves both risk and cost.

The third variant of efficiency measurement explores the change in the capacity utilization of fixed assets over a period of time. The data pertaining to capacity utilization was collected from the several volumes of the Public Enterprises Survey. To draw a more candid picture pertaining to utilization of fixed assets, as well as to measure the change in capacity utilization (CU) of fixed assets over a period of time, the fixed assets were grouped into four categories on the basis of their usage, i.e. CU of fixed assets below 50 percent, from 50 to 75 percent, from 75 to 100 percent and above 100 percent.

Capital structure practices assume vital significance in corporate financial management, as they influence both return and risk of equity owners of corporate enterprises. This part provides an insight into their capital structure practices and liquidity position. Total debt to total equity (TD/TE) was used to determine the capital structure practices; it is the relationship between borrowed funds and shareholders' funds/net-worth; shareholders' funds are equal to equity capital plus preference-capital plus reserves and surpluses minus accumulated deficit minus deferred expenditures not written-off. At the same time, total debt is inclusive of long and short-term debt (in the name of secured and non-secured loans and provisions); short-term advances are ostensibly short-term but are generally renewed year after year and hence serve the long-term needs of the firm.

Furthermore, the position of liquidity has been measured in terms of the current ratio (CR) and acid test ratio (ATR). The PSEs should maintain adequate liquidity in terms of satisfactory CR and ATR which depends on their access to sources of funds and ease with which these funds can be tapped in times of need. In general, sizeable numbers of PSEs in India have arrangements for short-term credit needs, say, in the form of bank borrowings/overdraft and cash-credit limits from banks which enables them to operate on the lower margin of working capital. This is reflected in the relatively lower current ratio (CR) as well as acid test ratio (ATR). It is important to mention that, conventionally, a CR of 2:1 and an ATR of 1:1 are considered satisfactory.

For the successful operation and productivity of PSEs, the government initiated a voluntary retirement scheme (VRS) in PSEs during the period 1988–2002 (a new scheme for VRS) to shed the excess manpower and to improve the age-mix and skill-mix. Simultaneously, in order to improve the quality of the manpower, several training programs are organized which update employee knowledge and skills. Thus, it is another equally important aspect related to assessing the productivity of capital per employee which is determined in terms of level of employment, sales efficiency and net income efficiency ratios.

Survey findings are predominantly based on 15 responses received from disinvested PSEs. All the analysis of the questionnaire survey is presented for the sample responding companies. Limited attempt has been made to generalize the results, since the sample size is low.

SECTION IV
DISINVESTED CENTRAL PSEs

This section assesses the financial performance of disinvested PSEs on the basis of the periods before and after the disinvestment (on a rolling basis) for all significant financial aspects. In brief, the section aims at testing the following hypothesis:
H1: Recommendations of various experts and committees, in terms of reforms have laid a positive impact in improving the performance of disinvested PSEs in India. Hence, it is hypothesized that disinvestment has improved the financial performance of PSEs.

Relevant data relating to disinvestment of PSEs has shown findings which are contrary to the expectations. A marginal decrease has been observed (Table 1 and Figures 1 to 5) in the mean values of profitability ratios during phase two *vis-à-vis* phase one. Likewise, declines in TATR, FATR and CATR have also been noted. However, it is gratifying to note that disinvested PSEs are able to decrease the man-power employed (pronounced in VRS) which is statistically significant as per paired t-test. Furthermore, Inventory holding period (a variant of efficiency, i.e. raw materials inventory holding period (RMIHP), work-in-process inventory holding period (WIPIHP) and finished goods inventory holding period (FGIHP)) also shows a marginal decline (statistically insignificant) in holding days of inventory after disinvestment.

A notable increase which is statistically significant during the second phase has been noted in the productivity ratios (sales efficiency and NIE) compared to the first phase. A decrease in leverage (TD/TA) and increase in liquidity ratios are also worth noting. The similar conclusions virtually follow based on median and quartile (Q1 and Q3) values (depicted in Appendix 1) except in the cases of RONW and NPM. It is hypothesized that disinvestment would pave the way for better capacity utilization. However, the actual findings are not in conformity with this normal expectation. For instance, capacity utilization of more than four-fifths (23 out of 29) of the PSEs have shown a decreasing trend (though not statistically significant) after disinvestment (Table 2).

Table 1: Mean Values of Key Financial Ratios of PSEs Opted for Disinvestment, 1986-87 to 2006-07

Variables	No. of firms Before (After)# 1	Mean Five Years: Before disinvest -ment 2	Mean Five Years: After disinvest -ment 3	Change in Mean 3-2	Paired difference of Mean 2-3	Paired sample t-test 4	Degree of freedom (df) 5	Significance level 6
Profitability Ratios (%)								
ROTA	38(38)	11.83	11.03	-0.8	0.8	0.72	37	0.47
ROCE	38(37)	14.04	13.64	-0.76	1.43	0.33	36	0.75
RONW	38(37)	13.58	12.34	-1.57	1.43	0.95	36	0.35
OPM	38(38)	15.49	13.67	-1.81	1.69	0.93	37	0.36
NPM	38(37)	8.54	7.91	-0.84	0.49	0.39	36	0.70
Efficiency Ratios (in times)								
TATR	37(37)	1.08	0.97	-0.11	0.11	1.87	36	0.07
FATR	35(35)	3.33	3.20	-0.13	0.13	0.43	34	0.67
CATR	37(37)	1.94	1.72	-0.22	0.22	2.12	36	0.04*
• DCP (in days)	37(38)	62.13	72.34	11.84	-8.20	-1.78	36	0.08
• RMIHP used cap 770 days	34(34)	197.2	177.08	-19	25.68	1.51	31	0.14
• RMIHP used cap 365 days	30(31)	147.56	136.97	-5.02	13.96	1.24	27	0.23
• WIPIHP (in days)	27(27)	23.71	22.16	-1.55	1.55	0.67	26	0.51
• FGIHP (in days)	31(31)	28.51	25.71	-2.8	2.80	1.47	30	0.15
Leverage (in times)								
TD/TE	38(37)	0.99	0.77	-0.23	0.19	1.49	36	0.15
Liquidity (in times)								
CR	38(37)	2.18	2.33	0.09	-0.15	-1.11	36	0.27
ATR	38(38)	0.9	1.08	0.18	-0.18	-1.75	37	0.09
Productivity/ Output								
Sales Eff. (%)	38(38)	36.97	72.66	35.69	-35.69	-3.18	37	0.00**
NIE (%)	38(38)	2.26	4.54	2.29	-2.29	-3.06	37	0.00**
No. of Employees	38(38)	18,191	16,842	-1,350	1,349.45	2.25	37	0.03 *

Notes: 1. PSEs having negative net-worth were excluded and RONW is based on net profit.
2. OPM and NPM stand for operating profit margin and net-profit margin on sales, respectively.
3. ROTA is based on earnings before interest and taxes (EBIT).
4. ROCE is based on operating profit which excludes non-operating incomes (or other incomes) from EBIT.
5. ** and * mark to the significant level at 1% and 5%, respectively.
6. # Firms in bracket refers to number of firms after disinvestment.
7.CR – current ratio, ATR – acid test, ratio, TD/TA – total debt/total assets, TD/TE – total debt/total equity, TATR – total assets turnover ratio, FATR- fixed assets turnover ratio, CATR-current assets turnover ratio, DCP- debtors Collection period, RMIHP- raw materials inventory holding period, WIPIHP – work-in-progress inventory holding period, FGIHP – finished goods inventory holding period, ROTA – return on total assets, ROCE – return on capital employed, RONW – return on net worth, OPM – operating profit margin, NPM – net profit margin, NIE – Net Income Efficiency, and Sales Eff. – sales efficiency.
8.CR consisting value 5 and above, ATR – 3 and above, TD/TA – 1 and above, TD/TE – 5 and above, RMIHP – 0, 770 days and above, DCP – 0, 270 days and above, TATR- 4 and above, CATR-6 and above, FATR-10 and above, RONW- plus/minus 50 percent, ROCE- plus/minus 50 percent, ROTA – plus/minus 35 percent, OPM – plus/minus 50 percent, and NPM – plus/minus 40 percent are eliminated.

These points hold true for other Tables mentioned in this section and other sections.

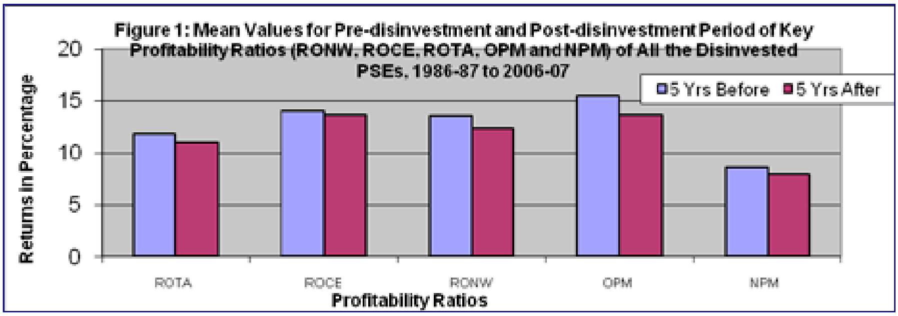


Figure 1: Mean Values for Pre-disinvestment and Post-disinvestment Period of Key Profitability Ratios (RONW, ROCE, ROTA, OPM and NPM) of All the Disinvested PSEs, 1986-87 to 2006-07

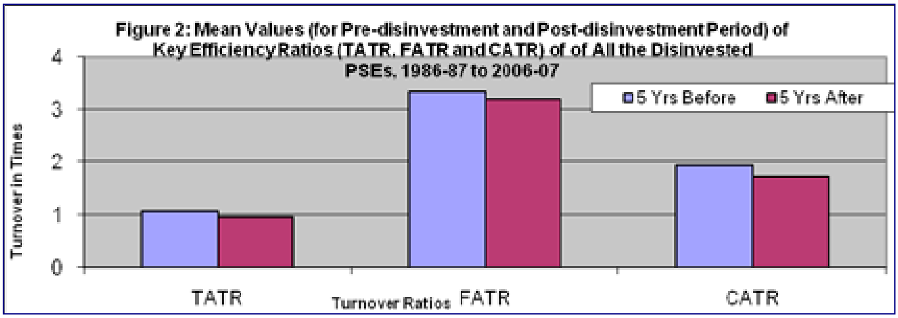


Figure 2: Mean Values (for Pre-disinvestment and Post-disinvestment Period) of Key Efficiency Ratios (TATR, FATR and CATR) of of All the Disinvested PSEs, 1986-87 to 2006-07

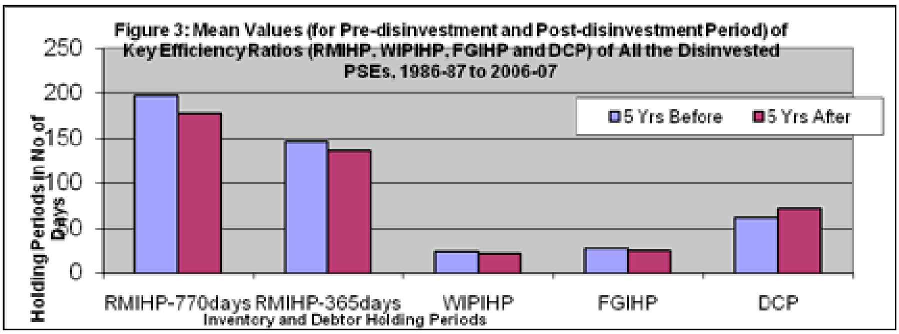


Figure 3: Mean Values (for Pre-disinvestment and Post-disinvestment Period) of Key Efficiency Ratios (RMIHP, WIPIHP, FGIHP and DCP) of All the Disinvested PSEs, 1986-87 to 2006-07

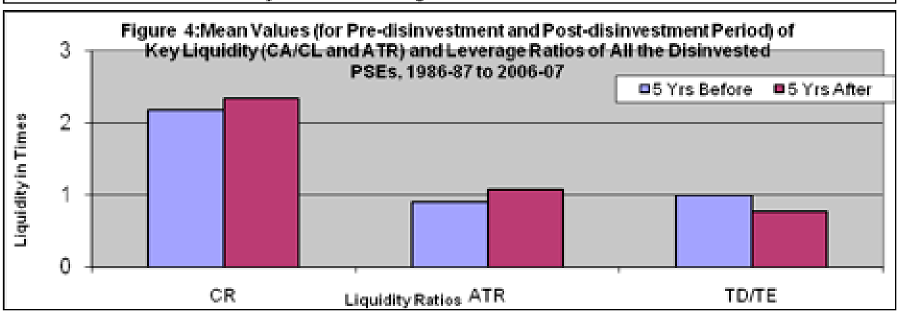


Figure 4: Mean Values (for Pre-disinvestment and Post-disinvestment Period) of Key Liquidity (CA/CL and ATR) and Leverage Ratios of All the Disinvested PSEs, 1986-87 to 2006-07

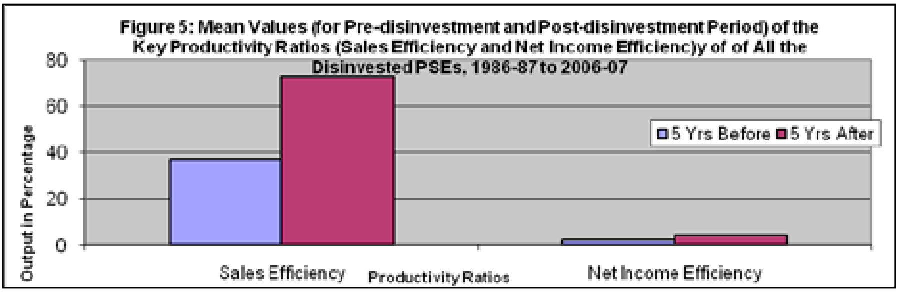


Table 2: Mean Values of Capacity Utilization Ratio of the Public Sector Enterprises (PSEs) Opted for Disinvestment, 1986-87 to 2006-07
(Figures are in percentage)

Capacity Utilization Ratio	No. of firms Before (After)# 1	Mean Five years		Change in Mean 3-2	Paired t-test for difference of Mean 4	Degree of freedom (df) 5	Firms showing better performance (%) 6	Significance level 7
		Before disinvestment 2	After disinvestment 3					
Below 50 %	2(2)	82.7	46.0	-36.7	36.70	1	0	0.48
More than 50 and less than 75%	8(8)	83.6	78.1	-5.5	5.50	7	63	0.47
More than 75 and less than 100%	13(13)	83.8	84.8	1.0	-0.98	12	70	0.78
More than 100%	6(6)	95.4	100.9	5.5	-5.50	5	83	0.42

Firms in brackets refer to number of firms after disinvestment

Table 3: Disinvested PSEs showing Improvement or Deterioration in Performance (Measured in terms of Profitability and Efficiency), 1986-87 to 2006-07

Variables	No. of firms Before (After)#	Firms showing Improvement in Performance (%)	Firms showing Deterioration in Performance (%)
Profitability			
ROTA	38(38)	45	55
ROCE	38(37)	41	59
RONW	38(37)	50	50
OPM	38(38)	45	55
NPM	38(37)	53	47

Efficiency			
TATR	37(37)	46	54
FATR	35(35)	46	54
CATR	37(37)	35	65
DCP	37(38)	40	60
RMIHP cap 770 days	34(34)	66	34
RMIHP cap 365 days	30(31)	71	29
WIPIHP	27(27)	63	37
FGIHP	31(31)	55	45

Firms in brackets refer to number of firms after disinvestment.

Findings are equally revealing with respect to profitability and efficiency measures of disinvested enterprises during the period of the study. In fact, the number of such firms showing deterioration in ROR is half or more in the second phase compared to the first phase; likewise, the decrease in all major efficiency ratios has been in a larger number of firms *vis-à-vis* the number of firms showing improvement (Table 3). Therefore, the findings do not support the hypothesis of improvement in financial performance of disinvested PSEs after disinvestment *vis-à-vis* before disinvestment (in a sizeable number of cases).

These findings are in conformity with other notable studies on the subject. For instance, Bishop and Kay (1989*)* found no strong evidence that indicated the privatized firms did better. Likewise, Abelson (2003) derived out of his nine case studies that long-term financial returns played very little part in the decision to privatize; there is a consistent pattern of winners and losers from the privatization; the winners were the financial institutions, the new shareholders and private consultants and the main losers were the future taxpayers and workers in the presale organizations.

Table 4: Decision-Making Approach in Financial Aspects in the Disinvested PSEs in India

Opinion	**Combined (out of 15)**	
	No.	%
Focused	3	21.4
Participative	10	71.4
Any other	1	7.2
Total	14	100%
Missing	1	

Table 5: Opinion on Enhancement of Management Power by the Government and its Positive Effect on Increasing the Profitability of Responding PSEs

Opinion	**Enhancement of Management Power by Government**		**Enhanced Power Increases Profitability**	
	No.	%	No.	%
Yes	13	86.7	12	92.3
No	2	13.33	1	7.7

Total	15	100.0%	13	100.0%
Missing			2	

Table 6: Preference for the Extent of Disinvestment that should take place in Sample PSEs

S.no	Options	Total PSEs Responded	Total PSEs Responded (%)
1	Below 25 % (as a policy matter)	1	7.7
2	Between 25-49%	3	23.1
3	Above 50% (private sector control)	9	69.2
	Total No. of Enterprises	13	100%
	Missing	2	

Table 7: Opinion on the Completion of Top Management Team Tenure and Chairman Compensation in Tune with Increases in Financial Performance in Sample PSEs in India

Opinion	Top Management Tenure		Chairman's Compensation	
	No.	%	No.	%
Yes	11	73.3	1	8.3
No	4	26.7	11	91.7
Total	15	100.0	12	100
Missing			3	

Table 8: Trend of Following Items in Disinvested Sample PSEs in India

Trend	Inventory Holding Period		Debtor Collection Period		Creditors Payment Period		Trend of Bad -Debt Losses	
	No.	%	No.	%	No.	%	No.	%
Increase	2	14.3	2	14.3	1	7.15	0	0
Decrease	7	50.0	7	50.0	8	57.15	6	50.0
Steady	5	35.7	5	35.7	5	35.7	6	50.0
Total	14	100%	14	100%	14	100%	12	100.0
Missing	1		1		1		3	

Table 9: Categorization of the Financial Objectives on the Basis of Importance in Disinvested Sample PSEs

Opinion	Maximize return on Investment		Desired Earning Per Share		Maximize Share Prices		Maximize Earnings	
	No.	%	No.	%	No.	%	No.	%
Very imp	13	86.7	10	66.7	6	40.0	13	86.7
Less imp	0	0	3	20.0	8	53.3	1	6.7
Not imp	2	13.3	2	13.3	1	6.7	1	6.7
Total	15	100%	15	100%	15	100%	15	100%

Imp=Important

Table 10: Usage of Inventories is Handled in the Disinvested Manufacturing and Service PSEs in India

S. no.	Options	Combined (out of 15)	
		No.	%
1	On the basis of demand forecast and expected sales	7	44.4
2	On the basis of production needs	8	55.6
	Total	15	100

Data from the questionnaire survey depicted in Tables 4 to 10 highlight that the majority of disinvested PSEs (more than seven-tenths) have opted for a participative approach in decision-making pertaining to financial aspects (Table 4), and nearly nine-tenths are of the opinion in favour of enhancing the management power which helps in increasing the profitability and performance of the enterprises (Table 5). More than four-fifths of the responding disinvested PSEs have either decreased or have shown steady trends in the collection period of debtors, in bad-debt losses and in inventory holding period (Table 8). This may be due to usage of inventories in nearly fifty percent of the enterprises on the basis of production needs (Table 10). As a result, the excess storage cost of inventories could be avoided. Similarly, the vast majority of disinvested PSEs have considered maximizing return on investment, desired earnings per share and maximizing earnings as very important objectives (Table 9). Large numbers of respondents (seventy percent) are not in favour of partial privatization (Table 6). Furthermore, incomplete tenure and improper compensation of top management in a majority of the cases de-motivate them which may adversely impact the companies' profitability (Table 7).

SECTION V
ON THE BASIS OF DEGREE OF DISINVESTMENT

The central objective of this section is to measure the impact of gradual disinvestment (or degree of disinvestment) on the financial and operating performance of the central PSEs. It is hypothesized that the higher quantum of disinvestment would yield better operating and financial performance. Dewatripont and Roland (1992*)* and Zsuzsanna, Kose and Abraham (1996) have examined the dynamics of privatization and provide an explanation for the different patterns of evolution of private ownership; they are able to distinguish characteristics of privatization in stages (experimentation) from those of partial privatization. Proponents of gradual privatization (Roland, 1994; Katz and Owen, 1995) claim that gradual privatization can make the transition process smoother and less painful and at the same time increase the chance for strong economic progress by taking advantage of the 'learning by doing' effect. Naib (2004) states that divestiture will result in shifting the objectives of owners and the type of incentive systems for management.

This section deals with the answer to multiple queries, such as whether higher disinvestment produces higher profitability and to what extent operational efficiency is related to the percentage of disinvestment, i.e. to what extent greater disinvestment generates higher liquidity, profitability and effective utilization of existing resources.

The impact of disinvestment has been measured by dividing degree of disinvestment into six segments, i.e. out of total share capital the percentage of disinvestment is a) up to 5 percent, b) between 5 and 10 percent, c) between 10 and 20 percent, d) between 20 and 30 percent, e) between 30 and 40 percent, and f) between 40 and 50 percent; the corresponding numbers of disinvested PSEs are 9, 8, 7, 4, 6 and 4, respectively. For each segment, mean values have been computed (on a before-after basis) for all the ratios. The ANOVA test has also been applied to determine the relations among them.

Disinvestment up to 5 percent

Table 11 indicates a moderate decline in profitability, efficiency and liquidity ratios of disinvested PSEs during the post-disinvestment *vis-à-vis* pre-disinvestment phase. *Inter-se,* sample PSEs witnessed a tremendous decrease in their mean profitability in the range of more than 15 percent (in the case of RONW) and up to 33 percent (in the case of NPM). A marginal increase in leverage (TD/TE) ratio has also been observed. In sum, no improvement due to disinvestment has been observed except in RMIHP, sales efficiency and NIE after disinvestment. The positive outcomes relates to the capacity utilization ratio. There has been an improvement in the case of a vast majority (four-fifths) of divested PSEs in the post-disinvestment phase.

Table 11: Mean Values of Key Financial Ratios of the PSEs on the basis of Extent of Disinvestment below 5 percent, between 5 and 10 percent and between 10 and 20 percent, 1986-87 to 2006-07

Ratios	Disinvestment below 5%			between 5 and 10%			between 10 and 20%		
	No. of firms Before (After)#	Mean Five Years		No. of firms Before (After)#	Mean Five Years		No. of firms Before (After)#	Mean Five Years	
		Before disinvest -ment	After disinvest -ment		Before disinvest -ment	After disinvest -ment		Before disinvest -ment	After disinvest -ment
	1	2	3	1	2	3	1	2	3
Profitability Ratios (in percentage)									
RONW	9(9)	11.75	10.24	8(7)	11.18	7.34	7(7)	12.73	14.00
ROCE	9(9)	10.61	8.35	8(7)	11.19	10.81	7(7)	10.50	14.50
ROTA	9(9)	11.35	8.88	8(8)	10.40	7.15	7(7)	9.61	12.78
OPM	9(9)	14.78	12.22	8(8)	14.26	8.71	7(7)	16.93	19.19
NPM	9(9)	9.74	6.18	8(8)	6.96	6.99	7(7)	9.89	11.26
Efficiency Ratios (in times)									
TATR	9(9)	1.06	0.96	8(8)	1.15	1.00	7(7)	0.93	0.87
FATR	8(8)	2.94	2.66	8(8)	3.74	3.53	7(7)	3.11	2.64
CATR	9(9)	1.70	1.61	8(8)	1.86	1.49	7(7)	1.92	1.92
• DCP (in days)	8(9)	56.49	72.72	8(8)	83.32	106.1	7(7)	41.88	38.71
• RMIHP _ 770 days	8(9)	249.3	152.0	8(6)	201.7	215.2	6(6)	223.7	196.3
• RMIHP _365 days	7(9)	204.9	152.0	6(5)	84.59	136.2	5(6)	153.2	167.4

• WIPIHP (in days)	6(6)	21.58	23.35	7(7)	25.52	21.29	3(3)	2.02	2.58
• FGIHP (in days)	7(7)	26.54	24.79	7(7)	36.87	27.33	5(5)	31.75	35.45
Capacity Utilization (in percentage)									
Below 50 %	1(1)	72.8	70.2	1(1)	92.6	21.8	0		
Between 50 and 75%	1(1)	74.6	85.0	3(3)	86.6	80.3	1(1)	105.4	79.6
Between 75 and 100%	3(3)	93.9	103.5	2(2)	92.5	88.5	2(2)	70.6	79.4
More than 100%	1(1)	74.0	93.4	0			2(2)	97.1	107.6
Leverage (in times)									
TD/TE	9(9)	0.71	0.75	8(7)	1.16	0.92	7(7)	1.04	0.96
Liquidity (in times)									
CR	9(9)	2.54	2.54	8(7)	2.35	2.09	7(7)	2.06	2.51
ATR	9(9)	1.12	1.09	8(8)	0.94	1.15	7(7)	0.96	1.06
Productivity/Output									
Sales Eff. (%)	9(9)	18.05	29.02	8(8)	28.93	42.86	7(7)	43.75	92.51
NIE (%)	9(9)	1.00	1.16	8(8)	0.83	1.27	7(7)	2.28	6.81
No. of Employees	9(9)	7,059	6,491	8(8)	10,866	9,941	7(7)	41,499	37,728

Disinvestment in the range of 5 to 10 percent

Relevant data contained in Table 11 pertaining to disinvested PSEs in the range of 5 to 10 percent depicts decreases in almost all the parameters of profitability, efficiency (assets turnover) and liquidity; increases were observed in holding periods of inventory and debtors after disinvestment; the positive notable features have been in respect to decreases in leverage ratios and increases in productivity ratios (in terms of sales efficiency and NIE).

There has been no improvement in the capacity utilization ratio of such PSEs resulting from higher disinvestment. In brief, the findings in the sub-section indicate that minor increases in the percentage of disinvestment (of 5 to 10 percent) do not yield better performance for disinvested PSEs.

Disinvestment in the range of 10 to 20 percent

The analysis shows that higher disinvestment (10 to 20 percent) brought improvement in the financial performance of PSEs. Table 11 presents notable increases in the primary measure of financial performance, i.e. profitability ratios. The increase varies from more than 10 percent (in RONW) to 40 percent (in ROCE)) during second phase compared to the first phase of disinvestment. Furthermore, significant decreases in leverage as well as increases in liquidity and productivity (in terms of sales efficiency and net-income efficiency) ratios were also observed during the same phase. Likewise, the values of capacity utilization indicate that four-fifths of the firms having capacity utilization in the range of above 75 percent to more than 100 percent improved their capacity after disinvestment. Deterioration in performance was observed only in the case of efficiency measures (decreases in assets turnover and increases in inventory holding period and debtor collection period).

Disinvestment from 20 to 30 percent

The findings are contrary to the normal expectation of better performance (with respect to profitability) with a higher quantum of disinvestment. Mean profitability declined (Table 12). As far as assets turnover, liquidity and productivity ratios are concerned, improvement was noted in all of them; likewise, there was a significant decrease in the inventory holding period (raw materials, work-in-process and finished goods) and the leverage ratio.

Capacity utilization suggests that 3 out of 4 disinvested sample enterprises decreased their capacity utilization during the second phase *vis-à-vis* the first phase. It may be recalled that better performance has been observed in PSEs having disinvestment ranging from 10 to20 percent. The findings in this sub-section do not reinforce the contention that disinvestment improves profitability. However, operational efficiency, liquidity and productivity positions did register marginal improvement.

Table 12: Mean Values of Key Financial Ratios of the Public Sector Enterprises on the basis of the Extent of Disinvestment between 20 and 30 percent, 30 and 40 percent, and 40 and 50 percent, 1986-87 to 2006-07

Ratios	Between 20 to 30%			Between 30 to 40%			Between 40 to 50%		
	No. of firms Before (After)#	Mean Five Years		No. of firms Before (After)#	Mean Five Years		No. of firms Before (After)#	Mean Five Years	
		Before disinvest-ment	After disinvest-ment		Before disinvest-ment	After disinvest-ment		Before disinvest-ment	After disinvest-ment
	1	2	3	1	2	3	1	2	3
Profitability Ratios (%)									
RONW	4(4)	10.98	6.67	6(6)	19.43	20.04	4(4)	17.82	17.00
ROCE	4(4)	15.09	11.84	6(6)	22.61	21.79	4(4)	19.72	18.55
ROTA	4(4)	10.03	9.01	6(6)	16.88	16.69	4(4)	13.87	14.13
OPM	4(4)	16.10	11.26	6(6)	13.76	14.70	4(4)	18.99	19.33
NPM	4(4)	7.53	2.38	6(6)	7.10	8.22	4(4)	9.79	12.60
Efficiency Ratios (in times)									
TATR	4(4)	0.63	0.75	5(5)	1.46	1.17	4(4)	1.18	1.07
FATR	4(4)	2.45	3.81	5(5)	4.48	4.33	4(4)	3.22	2.63
CATR	4(4)	1.23	1.24	6(5)	2.63	2.25	4(4)	2.56	1.92
• DCP (in days)	4(4)	95.62	101.9	6(6)	66.34	70.80	4(4)	26.69	35.56
• RMIHP _ 770 days	4(4)	223.1	232.5	5(6)	118.1	169.8	3(3)	90.57	78.41
• RMIHP 365 days	4(3)	205.7	152.3	5(5)	118.1	85.86	3(3)	90.57	78.41
• WIPIHP (in days)	4(4)	45.88	35.81	4(4)	27.60	32.90	3(3)	10.68	8.84
• FGIHP (in days)	4(4)	37.71	31.03	5(5)	12.36	13.54	3(3)	22.86	21.02
Capacity Utilization (%)									
Below 50 %	0			0			0		
Between 50 and 75%	1(1)	67.8	69.8	1(1)	79.0	64.5	1(1)	82.2	84.8

Between 75 and 100%	1(1)	79.6	53.8	3(3)	74.8	74.0	2(2)	89.0	90.4
More than 100%	2(2)	96.2	85.9	1(1)	111.8	125.0	0		
Leverage (in times)									
TD/TE	4(4)	1.01	1.00	6(6)	0.84	0.40	4(4)	1.34	0.59
Liquidity (in times)									
CR	4(4)	2.06	2.24	6(6)	1.72	2.09	4(4)	2.09	2.45
ATR	4(4)	0.81	0.96	6(6)	0.84	1.26	4(4)	1.10	3.28
Productivity/Output									
Sales Eff. (%)	4(4)	8.03	15.39	6(6)	96.79	196.6	4(4)	22.95	67.16
NIE (%)	4(4)	0.62	0.88	6(6)	7.88	14.64	4(4)	1.10	3.28
No. of Employees	4(4)	16,242	14,095	6(6)	17,428	15,886	4(4)	20,195	21,564

Disinvestment in the range of 30 to 40 percent

Table 12 indicates mixed results; marginal decreases in operational efficiency were observed in virtually all the parameters of assets turnover, inventory holding period and debtors collection period; capacity utilization of the resources also decreased in four-fifths of the sample PSEs. Though, figures related to the leverage, liquidity and productivity (sales efficiency and NIE) ratios showed better results after disinvestment; similarly, marginal increases in the three profitability ratios (RONW, OPM and NPM) were also recorded.

Disinvestment from 40 to 51 percent

Table 12 discloses a sizable increase in productivity and liquidity ratios and a marginal increase in three important measures of profitability (ROTA, OPM and NPM) during the post-disinvestment phase *vis-à-vis* the pre-disinvestment phase; similarly, decreases in the inventory holding period (with respect to all types of inventories) was observed during the same time frame. As far as assets utilization is concerned, there was a decline in all types of assets turnover ratios; although, the mean capacity utilization of the sample PSEs improved marginally after disinvestment. However, all are operating below 100 percent of their capacity.

The preceding analysis indicates mixed results among all the six groups related to the degree of disinvestment and various parameters of financial performance. For instance, there has been marginal improvement in a few parameters of profitability. The position of liquidity, leverage and efficiency (in terms of inventory holding period, sales efficiency and NIE) ratios show an improvement due to a higher amount of disinvestment in a majority of the cases. Other parameters, such as assets turnover (current as well as fixed, save 20 to 30 percent disinvestment) have a pronounced declining trend, and DCP reflects an increasing trend.

The findings in this part contradict the perception that higher disinvestment brings out higher efficiency or effectiveness in utilization of resources which in turn raises profitability at all levels. Koen (1998) suggested that privatization alone is not the answer for good governance; managerial skills, the existence of performance incentives, transparency and a sound legal system are also required. Gupta et al. (2000) stated that fiscal constraints seem to be the main motivating factor in choosing partial privatization, and this is consistent with the empirical findings. Abelson (2003) stated that long-term financial returns played very little part in the decision to privatize. Das (1999) expressed that, contrary to expectation, profitability, liquidity and assets turnover dropped instead of improving.

Furthermore, to examine the relationship and impact of the degree of disinvestment among the six groups, the one way analysis of variance (ANOVA) test was conducted (please refer to Appendix 2); it identified the significant difference in all the parameters of profitability (except OPM and NPM) and efficiency. Under liquidity and productivity, statistically significant difference was observed only in the CR and NIE which to a large extent corroborates to the hypothesis that better performance is associated with a higher degree of disinvestment.

SECTION VI
DISINVESTED PSEs ON THE BASIS OF ASSETS SIZE

This section examines the financial performance of disinvested PSEs based on the size of assets. For the purpose of analysis, the sample enterprises were categorized into four groups, namely micro, small, medium and large. The firms holding total assets of less than Rs. 1,000 crore (Rs. 10,000 million) are referred to as micro PSEs; small size disinvested PSEs are those which have the assets size between Rs. 1,000 to Rs. 3,000 crore (Rs. 10,000 to 30,000 million); PSEs having assets between Rs. 3,000 to Rs. 10,000 crore (Rs. 30,000 to 100,000 million) are referred to as medium size enterprises, and large size PSEs carry total assets above Rs. 10,000 crore (Rs. 100,000 million). It is expected that the size of assets has an impact on enhancing the financial performance of PSEs after disinvestment.

Disinvested PSEs having Total Assets less than Rs. 1,000 Crore

Table 13 deals with the disinvested PSEs with a total assets size less than Rs. 1,000 crore; a notable decline has been identified in the mean values of profitability, efficiency (in terms of fixed, current and total assets turnover ratios), productivity ratios (NIE and number of employees) and liquidity (CR) ratios during phase two in comparison to phase one. During the same time period, a marginal improvement was noted in terms of a reduction in the inventory holding period, i.e. RMIHP_770 days, WIPIHP and FGIHP, and in leverage as well as an enhancement in sales efficiency. It is important to note that the enhancement in sales efficiency is mainly due to the reduction in employment and an increase in the sales (value). The State Trading Corporation of India and Indian Tourism and Development Corporation are the organizations which are excluded from RMIHP_365 days during the pre-disinvestment phase (as their inventory holding periods are greater than the cap of 365 days).

Table 13: Mean Values of Key Financial Ratios of the Disinvested PSEs having Total Assets less than Rs. 1,000 and between Rs. 1,000 and 3,000 Crore, 1986-87 to 2006-07

Ratios	Total Assets less than 1000 crore			Between 1,000 and 3,000 Crore		
	No. of firms	Mean Five Years		No. of firms	Mean Five Years	
	Before (After)# 1	Before disinvest -ment 2	After disinvest -ment 3	Before (After)# 1	Before disinvest -ment 2	After disinvest -ment 3
Profitability Ratios (%)						
RONW	9(8)	11.25	6.45	16(16)	13.44	12.78
ROCE	9(8)	12.22	7.68	16(16)	13.76	14.44
ROTA	9(9)	11.58	5.80	16(16)	11.94	11.62
OPM	9(9)	14.14	4.40	16(16)	13.64	14.02
NPM	9(8)	7.11	3.09	16(16)	7.89	7.75
Efficiency Ratios (in times)						
TATR	9(9)	0.95	0.85	15(15)	1.16	1.03
FATR	8(8)	2.60	1.96	14(14)	3.69	4.14
CATR	9(9)	1.63	1.42	15(15)	1.92	1.63
• DCP (in days)	9(9)	66.92	79.81	15(16)	55.39	67.93
• RMIHP _ 770 days	9(8)	232.5	160.5	14(13)	163.0	130.5
• RMIHP _365 days	7(8)	140.4	150.3	10(11)	170.6	183.9
• WIPIHP (in days)	7(7)	27.85	24.15	13(13)	24.72	24.97
• FGIHP (in days)	7(7)	35.12	28.22	13(13)	28.60	24.53
Leverage (in times)						
TD/TE	9(8)	1.01	1.01	16(16)	0.76	0.55
Liquidity (in times)						
CR	9(9)	2.44	2.27	16(16)	2.28	2.35
ATR	9(8)	1.04	1.11	16(16)	0.95	1.04
Productivity/Output						
Sales Eff(%)	9(9)	15.97	22.56	16(16)	44.25	83.46
NIE (%)	9(9)	0.58	0.48	16(16)	2.02	3.96
No. of Employees	9(9)	7,669	7,067	16(16)	7,631	7,008

Disinvested PSEs having Total Assets in the range of Rs. 1, 000 to Rs. 3,000 Crore

Table 13 shows mixed results in the measures of profitability and efficiency (with respect to assets turnover and the holding/collection period of inventory and debtors) during the pre and post-disinvestment phases. FATR shows an increase in the utilization of fixed assets in a majority of the PSEs; whereas, decreases in current assets turnover is primarily due to increases in the collection period of debtors and the holding period of raw materials and work-in-process. Sizable improvement was recorded in productivity (nearly two times) and liquidity (more than the convention of 2:1 for liquidity and 1:1 for ATR) ratios. The reasons of low profitability in PSEs may be due to excessive investment in working capital (as per various studies conducted by the Bureau of Public Enterprises).

Table 14: Mean Values of Key Financial Ratios of the Disinvested PSEs having Total Assets between Rs. 3,000 to Rs. 10,000 and above Rs. 10,000 Crore, 1986-87 to 2006-07

Ratios	Between Rs. 3,000 and 10,000 crore			Above Rs. 10,000 crore		
	No. of firms Before (After)# 1	Mean Five Years Before disinvest-ment 2	Mean Five Years After disinvest-ment 3	No. of firms Before (After)# 1	Mean Five Years Before disinvest-ment 2	Mean Five Years After disinvest-ment 3
Profitability Ratios (%)						
RONW	6(6)	10.92	13.60	7(7)	19.18	16.97
ROCE	6(6)	10.72	10.71	7(7)	19.84	21.12
ROTA	6(6)	9.39	11.86	7(7)	13.99	15.71
OPM	6(6)	19.84	22.80	7(7)	17.72	17.68
NPM	6(6)	10.33	12.10	7(7)	10.32	10.17
Efficiency Ratios (in times)						
TATR	6(6)	0.56	0.55	7(7)	1.50	1.35
FATR	6(6)	2.25	2.54	7(7)	4.37	3.29
CATR	6(6)	1.28	1.19	7(7)	2.96	2.77
• DCP (in days)	6(6)	112.0	128.1	7(7)	27.67	25.06
• RMIHP _ 770 days	6(6)	292.1	257.9	5(5)	94.32	86.14
• RMIHP _365 days	4(5)	164.4	183.2	5(5)	94.32	72.10
• WIPIHP (in days)	4(4)	29.77	25.02	3(3)	1.57	1.49
• FGIHP (in days)	5(5)	23.93	22.24	6(6)	24.43	28.23
Leverage (in times)						
TD/TE	6(6)	1.41	1.07	7(7)	1.11	0.76
Liquidity (in times)						
CR	6(5)	1.96	2.52	7(7)	1.82	2.24
ATR	6(6)	1.03	1.51	7(7)	0.50	0.76
Productivity/Output						
Sales Eff(%)	6(6)	8.62	28.87	7(7)	71.62	149.9
NIE (%)	6(6)	0.87	2.78	7(7)	6.15	12.63
No. of Employees	6(6)	25,391	22,825	7(7)	49,686	46,757

Disinvested PSEs having Total Assets in the range of Rs. 3,000 to Rs. 10,000 Crore

Marginal increases were observed in the mean values of profitability and efficiency ratios, i.e. TATR and FATR, after disinvestments; in fact, performance of TATR is unsatisfactory inasmuch as it is less than one (almost one half) as per Table 14.

However, a fairly a good increase in liquidity and efficiency, i.e. sales efficiency and NIE, ratios as well as decreases in leverage and the inventory holding period were observed during phase two *vis-à-vis* phase one; *Prima-facie,* the CR and ATR of the sample enterprises itself are higher than the prescribed rule of thumb (2:1 for CR and 1:1 for ATR) which reflect excessive liquidity (for such PSEs) than required, weakening profitability is indicative of under-utilization of resources. In sum, it seems that a greater size of total assets contributes to enhancing the financial performance of the sample PSEs.

Disinvested PSEs having Total Assets above Rs. 10,000 Crore

This segment of the study analyses the performance of disinvested enterprises which are holding total assets above Rs. 10,000 crore primarily in terms of profitability and efficiency. The profitability ratio (mean) shows mixed results and efficiency (in terms of assets turnover) and a declining trend during the post-disinvestment phase *vis-à-vis* the pre-disinvestment phase (Table 14); during a similar time frame, marginal improvements (with respect to decreases in the number of days of the holding period) in the inventory holding period and substantial improvement in NIE and sales efficiency were observed. In fact, the liquidity ratios of all the PSEs seem to be high (more than the ideal standard) and use of debt (which is the cheapest source of finance) is low; it may have adversely affected the ROR for the net worth of these PSEs.

The results of one-way analysis of variance testing (ANOVA) conducted to test the alternate hypothesis (Ha: μ of micro size ≠ μ of small size ≠ μ of medium size ≠ μ large size) is presented in Appendix 3; the results clearly bring to the fore that the assets size has significant bearing on the financial performance of the disinvested PSEs in many of the parameters, i.e. profitability (RONW, ROCE and NPM) and efficiency (except FGIHP) ratios.

The following select empirical studies are worth quoting in the present context of our study: Naib (2004) contends that the vast investments have failed to produce the surpluses which they were expected to generate and the return on capital employed is quite low. Sueyoshi (1998) states that the Nippon and Telephone Ltd. privatization has enhanced productivity primarily due to reduction in personnel, otherwise it has failed to achieve any significant improvement in cost management even after privatization. Whereas Megginson and Netter (2001) conclude that increases in performance are associated with privatization, it appears to improve performance in many different ways in many different countries. Asian Development Bank (2001) suggests that for successful privatization, it is essential to define the roles and powers of participants and to ensure that legal, regulatory and enforcement mechanisms precede disinvestment.

SECTION VII
CONCLUDING OBSERVATIONS

The paper suggests that disinvestment brings no major improvement in some significant parameters, such as profitability, assets turnover and capacity utilization, even after five years of disinvestment; improvement has been noted with respect to productivity of capital and liquidity only. In fact, findings are not in conformity with normal expectations that disinvested PSEs perform better. Low profit margin, a competitive environment, administrative price control and declines in usage of debt have been listed as the probable reasons for the decrease in profitability of disinvested PSEs by the respondents to the survey; the majority of disinvested PSEs are not favourable to partial disinvestment as control remains with the government; it hampers faster decision-making, having an adverse impact on the performance of PSEs.

However, mixed results have been observed in the parameters of profitability among the six groups (based on the degree of disinvestment). The position of liquidity, leverage, inventory holding period (IHP) and productivity have shown improvement due to higher disinvestment. The ANOVA test also signifies a positive relation between the quantum of disinvestment with higher financial performance.

Likewise, assets sizes have disclosed positive performance in the parameters of efficiency (in terms of inventory holding period), leverage, liquidity and productivity with increases in assets size. The ANOVA test corroborates that assets size has a significant bearing on the financial performance of disinvested PSEs in a majority of the parameters.

In sum, it is reasonable to state that partial disinvestment has not derived the desired or expected results; it may be due to variety of problems faced by PSEs even after disinvestment, such as having an inefficient, high cost and non-competitive industrial structure, operational inefficiency due to a high degree of governmental interference, environment restrictions (delegation of operational and functional autonomy to the managers through performance contracts), less disinvestment (for filling fiscal deficit gaps) and capital market discipline. Sueyoshi (1998) enumerates that the performance and corporate behaviour of a firm cannot be determined only by its ownership but also by many external factors including the type of corporate environment (regulations and deregulations) and types of clients (government or private firms); a public firm facing serious competitors may behave as private firm, and a privatize firm under government regulation may still function like public firm. Hence, disinvested public enterprise needs major structural changes, including replacement of leadership, the existence of performance incentives, transparency and education for managers in order to successfully shift to creating competitive firms.

References

Abelson, Peter. Public Enterprise Disinvestment: Australian Case Studies, *Economic Record*, 79(244), pp.152-154, March, (2003).

Arnold, J., Javorcik, B., Lipscomb, M. and Mattoo, A. Services Reform and Manufacturing Performance: Evidence from India, July 14. Available at *http://molly.lipscomb.googlepages.com/India_Services_Liberalization708.pdf*, (2008).

Asian Development Bank, Special Evaluation Study on the Privatization of Public Sector Enterprises: Lessons for Developing Member Countries, *ADB Report*, December, (2001).

Basu, Prahlad K., Demystifying Privatization in Developing Countries, *Journal International Journal of Public Sector Management*, 7(3), pp. 44-55, (1994).

Bishop, Matthew R. and Kay John A., Privatization in United Kingdom: Lesson from Experiences, *World Development*, 17(5), pp. 643-657, (1989).
Boardman, Anthony and Vining, Aidan R. Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed, and State-Owned Enterprises, *Journal of Law and Economics*, 32(1), pp. 1-33, April, (1989).
Boubakri, Narjess and Cosset, Jean Claude. Financial and Operating Performance of Newly Privatized Firms: Evidence from Developing Countries, *Journal of Finance,* LIII (3), pp. 1081-1110, (1998).
Bradbury, Michael E. Government Ownership and Financial Performance in a Competitive Environment: Evidence from the Corporatization of the New Zealand Government Computing Services, *Asia Pacific Journal of Management*, 16(1), pp.157-172, (1999).
Das, D. Productivity Growth in Indian Manufacturing: An Application of Domer Aggregation, Paper Presented at the *Workshop on Measurement of Productivity in India*, Institute of Human Development, New Delhi, July 9-10, (1999).
Disinvestment Manual, *Disinvestment Commission Report*s, Department of Disinvestment- Manual.htm, (2007).
Dewatripont, M. and Roland, G. The Virtue of Gradualism and Legitimacy in the Transition to a Market Economy, *The Economic Journal*, 102 (411), pp.291-300, (1992).
Gitman, Lawerence J. *Principales of Managerial Finance*, XI Edition, Pearsons, New York, (2009).
Gouri, Geeta. The New Economic Policy and Privatization in India**,** *Journal of Asian Economies*, 8(3), pp. 455-479, (1997).
Government of India, *Public Enterprises Survey*, Vol.1, Department of Public Enterprises, Ministry of Heavy Industries and Public Enterprises, pp.67, New Delhi, (2002-03).
Gupta, N., Ham, J.C. and Svejnar, J. *Priorities and Sequencing in Privatization: Theory and Evidence from the Czech Republic*, Mimeo, The William Davidson Institute, University of Michigan, (2000).
Gupta, Nandini. Partial Privatization and Firm Performance, *The Journal of Finance,* LX(2), pp. 987-1015, **(**2005).
Hamid, Beladi and Chi-Chur, Chao. Environmental policy, comparative advantage, and welfare for a developing economy*, Environment and Development Economics,* 11 (5), pp 559 -568, (2006).
Hammer, Richard M., Hinterhuber, Hans H. and Lorentx, Justus. Privatization a Cure for all Ills? *Long Range Planning*, 22(6), pp. 19-28, (1989).
Helfert, Erich A. *Techniques of Financial Analysis: A Guide to Value Creation*, Eleventh Edition, Mcgraw Hill Irwin, New York, (2003).
Hoekman, Bernard, Mattoo, Aaditya, and Sapir, Andre. The Political Economy of Services Trade Liberalization: A Case for International Regulatory Cooperation, *Oxford Review of Economic Policy*, 23(3), pp. 367-391, (2007).
Jain, P.K. Assessing the Performance of a Development Bank, *Long Range Planning*, 22(6), pp.100-106, (1989).

Jain, P.K. and Yadav, Surendra S. *Financial Management Practices: A Study of Public Sector Enterprises in India,* Hindustan Publishing Corporation, New-Delhi, pp.191-209, (2005).

Karpoff, J.M. and Rice, E.M. Organizational Form, Share Transferability and Firm Performance, *Journal of Financial Economics*, 24(1), pp.69-105, (1989).

Katz, B.G. and Owen, J. Designing an Optimal Privatization Plan for Restructuring Firms and Industries in Transition, *Journal of Comparative Economics*, 21(1), pp.1-28, (1995).

Kaur, Parminder and Singh, Bhawandeep. *Disinvestment: An Acceleration of Growth, Economic Reforms in India: A Sectoral Analysis*, New Century Publication, New-Delhi, (2005).

Kay, J.A. and Thompson, D.J. Privatization: A Policy in Search of a Rationale, *The Economics Journal*, 96(381), pp.18-32, (1986).

Keswani, Aneel and Shackleton, Mark B. How Real Option Disinvestment Flexibility Augments Project NPV, *European Journal of Operational Research*, 168(1), pp.240–252, (2006).

Koen, Vincent. Poland: Privatization as the Key to Efficiency, The OECD Observer, *Organization for Economic Cooperation and Development*, Paris, No. 213, pp.30, (1998).

Kumar, S. Public Enterprise Policy and Reform Measures in the 1990s, *Management in Government*, XXII(2-3), pp.433-439, New Delhi, (1992).

Little, I.M.D. *A Critique of Welfare Economics*, Oxford University Press, (1952).

Lorch, K. Privatization through Private Sale: The Bangladeshi Textile Industry in R.Ramamurti and R.Vernon (eds), *Privatization and Control of the State-Owned Enterprises*, pp. 126-152, Washington, D.C., The World Bank, (1991).

Magginson, W.L. and Netter, J.M. From State to Market: A Survey of Empirical Studies on Privatization, *Journal of Economic Literature*, XXXIX(2), pp.321-89, (2001).

Martin, S. and Parker, D. Privatization and Economic Performance throughout the UK Business Cycle, *Managerial and Decision Economics*, 16(3), pp.225-237, (1995).

Megginson, William L., Nash, Robert C. and Van Randenborgh, Matthias. The Financial and Operating Performance of Newly Privatized Firms: An International Empirical Analysis, *Journal of Finance,* 49(2), pp. 403-452, (1994).

Naib, Sudir. *Disinvestment in India: Policies, Procedure, Practices,* Sage Publication New Delhi, (2004).

Ramamurti, R. Testing the Limits of Privatization: Argentine Railroads, *World Development*, 25(12), pp.1973-1993, (1997).

Ray, K.K. and Maharana, S. Restructuring PSEs through Disinvestment: Some Critical Issues, *Pratibimba*, Journal of MIS, 2(2), pp.56-62, (2002).

Roland, G. On the Speed and Sequencing of Privatization and Restructuring, *The Economic Journal*, 104(426), pp.158-1168, (1994).

Rumelt, R.P. *Strategy, Structure and Economic Performance*, Cambridge, Massachusetts, Harvard University Press, (1974).

Sueyoshi, Toshiyuki. Theory and Methodology Privatization of Nippon Telegraph and Telephone: Was It a Good Policy Decision? *European Journal of Operational Research,* 107(1), pp. 45-61, (1998).

Vadlamannati, Krishna Chaitanya. Explaining the Relationship between Privatization and Fiscal Deficit, Current Account Deficit, Trade Deficit in India - An Empirical Analysis, January 22, Available at SSRN: url=*http://ssrn.com/abstract=994716*, (2007).

Yip, George S., Devinney, Timothy M. and Johnson, Gerry. Measuring Long Term Superior Performance: The UK's Long-Term Superior Performers 1984-2003, Long Range Planning, 42(390-413), (2009).

Zsuzsanna, Fluck, Kose, John and Ravid, S. Abraham. Privatizing in Stages and the Dynamics of Ownership Structure, *Pacific-Basin Finance Journal*, 4(2-3), pp.277-296, (1996).

Appendix 1: Median and Quartiles Values of Key Financial Ratios of PSEs Opted for Disinvestment, 1986-87 to 2006-07

Variables	No. of firms Before (After)# 1	Median : Five years		Change in Median	Q1: Five years		Change in Q1	Q3 : Five years		Change in Q3
		Before disinvest-ment 2	After disinvest-ment 3	3-2	Before disinvest-ment 4	After disinvest-ment 5	5-4	Before disinvest-ment 6	After disinvest-ment 7	7-6
Profitability (%)										
ROTA	38(38)	10.86	9.11	-1.90	7.17	4.55	-5.48	16.03	18.06	3.78
ROCE	38(37)	12.65	10.72	-2.40	6.33	1.85	-9.17	19.25	28.68	10.2
RONW	38(37)	11.74	12.67	3.13	5.77	4.09	-5.61	20.34	22.94	3.97
OPM	38(38)	12.62	11.87	0.33	6.14	4.89	-6.28	21.32	25.21	2.92
NPM	38(37)	5.70	5.83	0.02	2.17	1.18	-3.37	15.82	16.77	2.29
Efficiency (in times)										
TATR	37(37)	0.81	0.69	0.02	0.48	0.51	-0.22	1.46	1.00	0.14
FATR	35(35)	2.46	2.34	0.11	1.19	1.04	-0.78	5.20	6.03	1.28
CATR	37(37)	1.46	1.37	-0.18	0.79	0.87	-0.41	2.68	2.06	0.14
• DCP (in D*)	37(38)	43.56	45.85	4.12	14.68	18.09	-3.76	95.05	130.7	26.1
• RMIHP	28(29)	102.5	117.7	-15.4	66.12	47.11	-49	246.03	203.4	15.7
• WIPIHP	27(27)	9.54	6.23	-0.27	1.13	1.27	-4.28	49.26	48.78	1.27
• FGIHP (in D*	31(31)	18.83	19.37	-0.37	11.59	12.08	-4.86	41.72	40.25	2.55
Leverage (in times)										
TD/TE	38(37)	0.75	0.39	-0.15	0.28	0.12	-0.34	1.70	1.27	0.01
Liquidity (in times)										
CR	38(37)	1.98	2.22	0.05	1.36	1.39	-0.37	3.01	3.49	0.41
ATR	38(38)	0.86	0.92	0.11	0.35	0.48	-0.09	1.48	1.71	0.61
Productivity/Output										
Sales Eff(%)	38(38)	7.59	14.78	7.72	3.79	6.99	3.32	43.57	89.08	34.6

NIE (%)	38(38)	0.82	1.35	0.76	0.18	0.27	0.02	1.89	4.65	2.28
Employ-ment	38(38)	7,754	7,408	131	2,558	2,940	-827	19,063	17,910	295

Appendix 2: ANOVA Results of the Disinvested PSEs on the basis of Degree of Disinvestment, 1986-87 to 2006-07

Parameters		Sum of Squares	df	Mean Square	F	Sig.
RONW	Between Groups	199.92	5	39.98	12.54	0.00**
	Within Groups	19.13	6	3.19		
ROCE	Between Groups	246.39	5	49.28	17.47	0.00**
	Within Groups	16.93	6	2.82		
ROTA	Between Groups	94.43	5	18.89	8.14	0.01**
	Within Groups	13.93	6	2.32		
OPM	Between Groups	87.22	5	17.44	3.13	0.10
	Within Groups	33.44	6	5.57		
NPM	Between Groups	53.98	5	10.80	2.58	0.14
	Within Groups	25.11	6	4.19		
TATR	Between Groups	0.45	5	0.09	7.35	0.02*
	Within Groups	0.07	6	0.01		
FATR	Between Groups	3.87	5	0.77	3.62	0.07
	Within Groups	1.28	6	0.21		
CATR	Between Groups	10.52	5	2.10	27.52	0.00**
	Within Groups	0.46	6	0.08		
RMIHP	Between Groups	29,677.62	5	5,935.52	5.35	0.03*
	Within Groups	6,654.71	6	1,109.12		
WIPIHP	Between Groups	1,923.64	5	384.73	29.94	0.00**
	Within Groups	77.11	6	12.85		
FGIHP	Between Groups	696.72	5	139.34	10.64	0.01**
	Within Groups	78.58	6	13.10		
DCP	Between Groups	7,564.67	5	1,512.93	19.51	0.00**
	Within Groups	465.20	6	77.53		
TD/TE	Between Groups	0.30	5	0.06	0.89	0.54
	Within Groups	0.41	6	0.07		
CR	Between Groups	0.83	5	0.17	5.48	0.03*
	Within Groups	0.18	6	0.03		
ATR	Between Groups	0.32	5	0.06	1.93	0.22
	Within Groups	0.20	6	0.03		
Sales Efficiency	Between Groups	23,816.34	5	4,763.27	3.90	0.06
	Within Groups	7,331.33	6	1,221.89		
NIE	Between Groups	164.89	5	32.98	5.55	0.03*
	Within Groups	35.63	6	5.94		

Appendix 3: ANOVA Results of the Disinvested PSEs on the basis of various groups of Total Assets Size, 1986-87 to 2006-07

Parameters		Sum of Squares	df	Mean Square	F	Sig.
RONW	Between Groups	87.03	3	29.01	6.53	0.05*
	Within Groups	17.77	4	4.44		
ROCE	Between Groups	138.10	3	46.03	16.21	0.01**

	Within Groups	11.36	4	2.84		
ROTA	Between Groups	39.92	3	13.31	2.50	0.20
	Within Groups	21.29	4	5.32		
OPM	Between Groups	160.62	3	53.54	4.13	0.10
	Within Groups	51.89	4	12.97		
NPM	Between Groups	44.81	3	14.94	6.18	0.05*
	Within Groups	9.67	4	2.42		
TATR	Between Groups	0.80	3	0.27	42.83	0.00**
	Within Groups	0.02	4	0.01		
FATR	Between Groups	4.73	3	1.58	6.78	0.05*
	Within Groups	0.93	4	0.23		
CATR	Between Groups	8.08	3	2.69	96.26	0.00**
	Within Groups	0.11	4	0.03		
RMIHP	Between Groups	34,546.8	3	11,515.6	13.9	.01**
	Within Groups	3298.7	4	824.6		
WIPIHP	Between Groups	910.58	3.00	303.53	66.85	0.00**
	Within Groups	18.16	4.00	4.54		
FGIHP	Between Groups	75.49	3	25.16	2.47	0.20
	Within Groups	40.74	4	10.18		
DCP	Between Groups	8968	3	2,969	40.80	0.00**
	Within Groups	293.11	4	73.28		
TD/TE	Between Groups	0.41	3	0.14	5.33	0.07
	Within Groups	0.10	4	0.03		
CR	Between Groups	0.66	3	0.22	2.44	0.20
	Within Groups	0.36	4	0.09		
ATR	Between Groups	0.43	3	0.14	3.69	0.12

** and * stand for significance level at 1 percent and 5 percent, respectively.

Advancing Human Rights at the Corporate Level: New Challenges and Opportunities

Iradj Roberto Eghrari[25]

Abstract: The objective of this paper is to review the United Nations' guidelines on business and human rights as well as to offer some insights on how the newly-established Working Group on the issue of human rights and transnational corporations and other business enterprises, appointed by the UN Human Rights Council, can assist the corporate sector in implementing these guidelines.

Key words: human rights, corporate sector, business and human rights, guidelines, analysis, Human Rights Council, United Nations' guidelines, Guiding Principles, "Protect, Respect and Remedy" Framework.

Historical Background

Since the end of the Second World War, a large number of companies have expanded their operations to include working in developing countries. With the end of the Cold War, additional new markets brought both opportunities for expansion and challenges that included the need to deal with different cultures, governments and, most remarkably, human rights standards. From the standpoint of the populations, having foreign corporations come to their countries to explore cheap manpower and economic advantages is certainly a hint that their human rights are not as important as the human rights of others – by itself consists of a complete abuse of the international human rights statutes.

Seen from the angle of the corporations, on the other hand, even if there was no regard for human rights, there are several setbacks in this scenario that interfere with the success of their businesses. As noted by Chandler[26], "[w]ithout appropriate policies for the challenges they confront, [companies] have shown themselves liable to suffer significant damage not only to plant and personnel, but also to reputation, as has been the experience of a number of leading companies."

In attempts to solve this situation, a large number of voluntary initiatives were undertaken by companies and organizations in the decades during and after the Cold War, such as the OECD Guidelines for Multinational Enterprises (1976), the ILO Tripartite Declaration of Principles Concerning Multinational Enterprises and Social

[25] Member of the Brazilian National Human Rights Education Committee and Executive Director, Ágere – Cooperação em Advocacy

[26] CHANDLER, 2003.

Policy (1977), the Caux Principles for Business (1994), the US Model Business Principles (1996), the Global Sullivan Principles (1999), the UN Global Compact (2000), and the US-UK Voluntary Principles on Security and Human Rights (2000), which sought to establish the basis for the relation between businesses and human rights.

However, as stated by Avery, Short and Regaignon, the framework available thus far (which lacked corporate accountability at the international level presented varying and often weak systems of accountability within states, thus relying on voluntary measures by companies) was not able to address extensive human rights abuses.

“While voluntary codes and initiatives have been helpful in raising awareness of human rights issues and improving the conduct of some companies, at the end of the day voluntary codes are respected only by those firms that want to respect them. Respect for internationally accepted, fundamental human rights standards is mandatory, not voluntary.”[27]

Without a clear set of guidelines to follow, the companies were left to their own discretion in terms of how and when to adopt human rights standards in their operations. “Both the Global Compact and the OECD Guidelines state that companies should respect human rights,” said Chandler, “but neither document explains what this means”[28].

From ‘Norms’ to ‘Guiding Principles’

In 2003, the United Nations Commission on Human Rights adopted a document known as Norms on Business and Human Rights[29]. Even though there were several opportunities for member states and other stakeholders to contribute to the discussions that led to the adoption of this set of norms, there was a great amount of criticism towards it. This was largely because of the language it introduced and of concepts related to obligations and responsibilities on the part of the business sector, which were considered improperly “legally binding”. In a commentary that illustrates the level of frustration with and opposition to these norms, the United States Council for International Business (USCIB) stated that:

“the ‘norms’ extend far beyond issues of basic human rights and cover a wide range of political, social, and economic rights that are appropriately decided by national governments. It would be highly inappropriate to, in effect, privatize the policing of those rights by making companies the enforcing agent. (...) while well

---

[27] AVERY, SHORT and REGAIGNON, 2005.
[28] CHANDLER, 2003.
[29] E/CN.4/Sub.2/2003/12/Rev.2.

intentioned, this approach would be counterproductive because it risks undermining the resources and attention necessary to improve the capacity of national governments to implement and enforce their existing human rights laws, with which all companies – foreign or domestic, local or global – must already comply."[30]

In response, there were several articles and commentaries that sought to clarify the notions that were being pushed forward by the opponents of the norms. Chandler countered the statements by the USCIB and defended the need to go beyond the respect for national legislation:

"The USCIB says 'the Norms are predicated on the belief that human rights can best be advanced by circumventing national political and legal frameworks'. Not so. The first and most important paragraph of the Norms declares that 'States have the primary responsibility to respect, ensure respect for, prevent abuses of, and promote human rights recognized in international as well as national law, including ensuring that transnational corporations and other business enterprises respect human rights'."[31]

Avery, Short and Regaignon's article also calls for the adoption of standards that can be universally applied, stressing the shortcomings of national legislation that have allowed, and even promoted, discrimination and human rights violations:

"National law is not the human rights floor. It is surprising that a few companies still argue that if they respect national laws, that is enough. If one accepts this argument, it would have been enough for a company to respect the laws of Nazi Germany, or of apartheid South Africa. National law and practice are sometimes contrary to internationally accepted human rights standards. (…) There is a need to spell out clearly for business people what these human rights instruments require of their firms."[32]

In order to address this generalized discontentment in a manner that would bring the clarifications that the business sector required, the Commission decided to recommend that the Secretary-General appoint a Special Representative to deal with the issue. His task was "to identify and clarify standards of corporate responsibility and accountability regarding human rights; elaborate on state roles in regulating and adjudicating corporate activities; clarify concepts such as 'complicity' and 'spheres of influence'; and to develop methodologies for human rights impact assessments and consider state and corporate best practices"[33].

The recommendation was followed by Secretary-General Kofi Anan who appointed

[30] USCIB.

[31] CHANDLER, 2003.

[32] AVERY, SHORT and REGAIGNON, 2005.

[33] RUGGIE, 2009

Professor John Ruggie to a three-year mandate, beginning in July 2005; this mandate was later renewed for another three years by Secretary-General Ban Ki Moon. After extensive consultations with businesses, governments, and civil society, the Special Representative concluded that progress could only be achieved in the realm of business and human rights if it would be possible to establish a common framework of understanding that could be adopted by all stakeholders.

It was with this objective in mind that, in 2008, the Special Representative proposed to the Human Rights Council a policy framework based on three complementary and interdependent pillars: the **state duty to protect** against human rights abuses by third parties, including business; the **corporate responsibility to respect** human rights; and the need for greater access by victims to **effective remedy,** judicial and non-judicial. This is known as the "Protect, Respect and Remedy" Framework[34], and was unanimously welcomed by the member-states.

"Each pillar is an essential component in an inter-related and dynamic system of preventative and remedial measures: the State duty to protect because it lies at the very core of the international human rights regime; the corporate responsibility to respect because it is the basic expectation society has of business in relation to human rights; and access to remedy because even the most concerted efforts cannot prevent all abuse."[35]

Resolution A/HRC/RES/8/7 asked that the Special Representative operationalise the Framework, that is, "provide views and concrete and practical recommendations[36]" for its implementation. During the interactive dialogue held at the Council's June 2010 session, delegations decided that this operationalisation would require the definition of "Guiding Principles" which would establish "a common global platform for action, on which cumulative progress can be built, step-by-step, without foreclosing any other promising longer-term developments"[37].

As stated by the Special Representative in his final report[38],

"The Guiding Principles' normative contribution lies not in the creation of new international law obligations but in elaborating the implications of existing standards and practices for States and businesses; integrating them within a single, logically coherent and comprehensive template; and identifying where the current regime falls short and how it should be improved."

[34] A/HRC/8/5
[35] A/HRC/17/31, paragraph 9
[36] A/HRC/RES/8/7
[37] A/HRC/17/31, paragraph 13
[38] A/HRC/17/31, paragraph 14

For this purpose, each of the three pillars of the Framework was assigned with a set of foundational and operational principles, all accompanied by an explanatory commentary that further clarifies "its meaning and implications"[39]. For the purpose of illustration, we will look at one of the foundational principles related to corporate responsibility to respect human rights, which states:

"15. In order to meet their responsibility to respect human rights, business enterprises should have in place policies and processes appropriate to their size and circumstances, including: (a) A policy commitment to meet their responsibility to respect human rights; (b) A human rights due-diligence process to identify, prevent, mitigate and account for how they address their impacts on human rights; (c) Processes to enable the remediation of any adverse human rights impacts they cause or to which they contribute.[40]"

The commentary that follows this paragraph stresses that "business enterprises need to know and show that they respect human rights", and that in order to do this they need to have "policies and processes in place"[41]. The further elaboration as to what these policies and processes should tend to is provided in the "operational principles" described in the following section of the document. An example of these operational principles is given below:

"**Policy commitment**

16. As the basis for embedding their responsibility to respect human rights, business enterprises should express their commitment to meet this responsibility through a statement of policy that: (a) Is approved at the most senior level of the business enterprise; (b) Is informed by relevant internal and/or external expertise; (c) Stipulates the enterprise's human rights expectations of personnel, business partners and other parties directly linked to its operations, products or services; (d) Is publicly available and communicated internally and externally to all personnel, business partners and other relevant parties; (e) Is reflected in operational policies and procedures necessary to embed it throughout the business enterprise."

Once again, the commentary[42] to this section offers an opportunity for stakeholders to better understand certain elements which were put forward in the operational principles stated above. In this particular case, it gives a definition of the meaning of the term "statement", which is "used generically to describe whatever means an enterprise employs to set out publicly its responsibilities, commitments, and expectations"; defines that "the level of expertise required to ensure that the policy

[39] Idem.
[40] A/HRC/17/31 Annex, page 15.
[41] Idem.
[42] Idem.

statement is adequately informed" is not the same for all business enterprises, and will vary according to the complexity of its operations; recommends that the statement of commitment be made "publicly available" and "communicated actively to entities with which the enterprise has contractual relationships", as well as to "others directly linked to its operations" and to "potentially affected stakeholders", "in the case of operations with significant human rights risks"; and so forth.

Even though there is a great deal of detail provided by the Special Representative through the Guiding Principles in terms of what is expected from all stakeholders, he was careful enough to stress, in his final report, that each case has to be seen in its peculiarities and context:

"The Guiding Principles are not intended as a tool kit, simply to be taken off the shelf and plugged in. While the Principles themselves are universally applicable, the means by which they are realized will reflect the fact that we live in a world of 192 United Nations Member States, 80,000 transnational enterprises, 10 times as many subsidiaries and countless millions of national firms, most of which are small and medium-sized enterprises. When it comes to means for implementation, therefore, one size does not fit all."[43]

The Special Representative's final report, as well as its Annex containing the Guiding Principles, was approved by the Human Rights Council on 6 July 2011. But the real task of enforcing this Framework and gaining the respect and the collaboration of the corporate sector rest with the Working Group appointed by the Human Rights Council[44].

Looking forward: the Role of the Working Group on Business and Human Rights

With the termination of the mandate of the Special Representative, several challenges remain to be faced by the Working Group. As stated by Professor Ruggie in his Recommendations on Follow-Up to the Mandate, the Guiding Principles "will be new, at some risk of misinterpretation, and in need of mainstreaming into organizations and disseminating globally. This will require capacity building and advisory efforts in order to sustain and fully realize the potential generated by the Framework and the Guiding Principles."[45]

A careful examination of the responsibilities[46] attributed to the Working Group will be helpful in identifying the main challenges this body will face during its three-year mandate.

[43] A/HRC/17/31, paragraph 15
[44] A/HRC/RES/17/4
[45] RUGGIE, 2011
[46] A/HRC/RES/17/4, paragraph 6.

(a) To promote the effective and comprehensive dissemination and implementation of the Guiding Principles – In order to fulfil this responsibility, the Working Group can benefit from working together with the Office of the High Commissioner for Human Rights (OHCHR), with UNESCO and with national institutions of human rights, focusing especially on human rights education activities. UNESCO can also be an important partner in assisting with the identification of business forums that have developed an ongoing discussion on issues related to human rights, which can be invited to collaborate for the dissemination and implementation of these Guiding Principles. These forums will ultimately be able to influence the mindset of the companies to understand the importance of taking on the responsibility of respecting and protecting human rights.

(b) To identify, exchange and promote good practices and lessons learned on the implementation of the Guiding Principles and to assess and make recommendations thereon and, in that context, to seek and receive information from all relevant sources, including governments, transnational corporations and other business enterprises, national human rights institutions, civil society and rights-holders – In attempting to respond to this demand, it is the tendency of contemporary organizations to focus on the creation of a website to which stakeholders can submit their good practices and lessons learned in an open and self-regulated platform that allows random as well as guided interactions between them. Although this kind of practice may stimulate exchange to some extent, it is important that is complemented with an ongoing process of human rights education inside the companies and organizations. This essential element will transfer to the establishment a culture of seeking these good practices, sharing knowledge and improving the human rights conditions for all associates.

(c) To provide support for efforts to promote capacity-building and the use of the Guiding Principles, as well as, upon request, to provide advice and recommendations regarding the development of domestic legislation and policies relating to business and human rights – Building the capacities of all those involved in the processes in business-related activities is also intimately associated with human rights education campaigns and programs inside the working environment. These should focus on enhancing the participants' understanding of basic human rights issues (including specific treaties and other legal frameworks related to their areas of work) and of how these impact not only the reality of the corporate sector, but each participant's private life.

(d) To conduct country visits and to respond promptly to invitations from states – It is of utmost importance that the country visits focus solely on neither unveiling situations of human rights violations nor on celebrating good practices; they must balance between these two objectives. It should be born in mind that there is a great risk that official reports highlight only the good experiences and leave out the challenges and setbacks that have been encountered by private and public sector organizations. In order to avoid this pitfall, the Working Group must have a strong articulation with civil society organizations to facilitate access to their thematic and geographic reports. Close interaction with the OHCHR, Special Procedures mandate holders and with national institutions will allow the Working Group to establish an ongoing dialogue with the corporate sector at the country level, based on a fair and actual assessment of the human rights reality in each country.

(e) To continue to explore options and make recommendations at the national, regional and international levels for enhancing access to effective remedies available to those whose human rights are affected by corporate activities, including those in conflict areas – In terms of effective remedies, the Working Group must put its energy into assisting corporations to abide by the recommendations offered by Professor Ruggie, especially those concerning the implementation of non-judicial grievance mechanisms at the company level that "operate through dialogue and engagement rather than the company itself acting as adjudicator of its own actions"[47]. Moreover, in all evaluations of good practices related to the grievance mechanisms, the principles of legitimacy, accessibility, predictability, rights-compatibility, equitability and transparency must be observed.

(f) To integrate a gender perspective throughout the work of the mandate and to give special attention to persons living in vulnerable situations, in particular to children – A growing percentage of the world's population is now living in contexts of climate change, natural disasters and/or internal conflicts that leave them in situations where it is not affordable for them to make professional or individual choices based on their preferences – they have to settle for what is available to them at a certain circumstance. This is especially the case for women and children, who in many parts of the world are left when all the men set off to seek better opportunities. At the same time, going beyond the recognition that women and persons living in vulnerable situations need special attention requires a broader understanding of their roles and potentials in human society. Offering an environment and opportunities that will allow them to participate as subjects capable of contributing to the advancement of society (including in all fields of work) will enable companies to view their own potentialities through a different perspective. Also, allowing males opportunities to participate more in the dynamics of the household and in care-giving contexts will assist them in understanding their own responsibilities towards the community and, consequently, towards the work environment.

[47] RUGGIE, 2008.

(g) To work in close cooperation and coordination with other relevant special procedures of the Human Rights Council, relevant United Nations and other international bodies, the treaty bodies and regional human rights organizations; and

(h) To develop a regular dialogue and discuss possible areas of cooperation with governments and all relevant actors, including relevant United Nations bodies, specialized agencies, funds and programs, in particular the Office of the United Nations High Commissioner for Human Rights, the Global Compact, the International Labor Organization, the World Bank and its International Finance Corporation, the United Nations Development Program and the International Organization for Migration, as well as transnational corporations and other business enterprises, national human rights institutions, representatives of indigenous peoples, civil society organizations and other regional and sub-regional international organizations – As stated under item (a), it will only be possible for the Working Group to protect the substantial achievements realized under the mandate of the Special Representative and to advance practical progress on the ground if this work is done in collaboration and cooperation with UN agencies and bodies as well as with regional, national and international bodies that deal with issues related to human rights. As stated by the Special Representative in his final recommendations, the foundation for better managing the challenges going forward is to secure "wide multi-stakeholder support for the 'Protect, Respect and Remedy' Framework and the Guiding Principles for its implementation"[48].

The Working Group is also asked (i) to guide the work of the Forum on Business and Human Rights established pursuant to paragraph 12 of the Resolution; and (j) to report annually to the Human Rights Council and the General Assembly.

Possible implications for state-owned organizations

Throughout the world, there is growing concern over public companies which are managed by state institutions. During a High Level Meeting of the State Ownership Authorities promoted by the International Centre for Promotion of Enterprises (ICPE) in September 2011 in Ljubljana, Slovenia, Maria Vagliasindi, leading economist of the Department of Sustainable Energy at the World Bank, gave an interview in which she commented on the differences between state-owned companies and private companies.

[The difference] "is that the first have more goals, which are, on various occasions, in conflict. (…) the goal of state-owned companies should be the same as that of the private ones, that is to maximize profit, which is the only way to acquire capital for new investments. But state-owned companies have to, at the same time, be careful to

[48] RUGGIE, 2011.

offer their products for a good price, accessible to their citizens. The difficult part is to achieve both of these goals."[49]

Vagliasindi also stated that, although said state-owned companies can be "prone to corruption and non-transparency, they can pursue social goals which are usually not interesting for private owners because they would probably not be lucrative enough". The challenge, then, is how to "introduce rules of corporate governance" into the management of public organizations, while at the same time ensuring that the role of the state be more than just the maintenance of power, but also focus on providing better services and improving the companies.

Following the same line of thought, the Director General of ICPE, Dr. Štefan Bogdan Šalej, stated at this same occasion that poor management of state-owned enterprises is bad for both the national governments and for society at large, as it increases poverty. He stressed that the goals of a state-owned company must be separated from the political agendas of the government in power, and that "the state can be a good owner, if it is a responsible owner".

"what is (…) important is to have a clear vision and objectives. We cannot achieve good results if we don't know what we want or if the political interests prevail over national ones"[50].

While these quotes do not relate directly to the discussions of business and human rights, it is interesting to note that the views expressed at the meeting in Ljubljana bring in the components of ameliorating services for the population, alleviating poverty and pursuing social goals. In this sense – although it was agreed by most participants in that meeting that the challenges in the management of state-owned companies will be much more difficult that the ones related to the reform of private companies – it is our belief that the adoption of Ruggie's Guiding Principles to this area of enterprise can also have good results in the long run.

The so-called "rules of corporate governance" to which Vagliasindi referred cannot be isolated from the entirety of the business sector and its responsibility towards the Protect, Respect and Remedy Framework. Indeed, in terms of state-owned enterprises there are implications not only for the state (which is expected to protect human rights) but also for the business itself, which must respect those rights and offer both judicial and non-judicial grievance mechanisms to any individuals or groups whose rights have been violated in consequence of their involvement with the company, its products or the policies it implements.

[49] ICPE, 2011.
[50] Idem

Concluding thoughts

It is clear that there is a long way to go in terms of establishing an equilibrium between the private interests of the corporate sector and human rights. At the same time, numerous studies have concluded that good management does not imply a mere financial calculation of money invested, saved and made by companies; it also has to do with the impact that the businesses have in society at large and with how these investments in social welfare and human rights can, in turn, have positive effects over the economic results as well.

While in the early 2000s there was a great deal of suspicion regarding human rights in business, the extensive work of the Special Representative has been able to open doors for dialogue among a diversity of stakeholders, clarifying a vision that the responsibility of observing human rights falls over all areas of human enterprise.

The lessons occurring since the adoption of voluntary commitments, such as the Global Compact and others, have added to the rich discussions derived from the adoption of the United Nations 'Norms' on business and human rights, and now with the approval of the Guiding Principles proposed by Ruggie, they have allowed the corporate sector to evaluate its role in the advancement of civilization. Investing in the well-being of employees, collaborators, suppliers and the community has proved to have more positive effects in the medium and long terms than having to deal with all the consequences of poor, self-interested management.

The challenge of adapting management strategies of state-owned organizations to suit the Guiding Principles is not a small one. To begin with, these public companies must be included in the pool of organizations with whom the Working Group will interact. Sharing good practices and involving these stakeholders in the dialogue is a first step in assisting the establishment of substantial changes in terms of the way they fit into this ever more integrated and inter-related world, guaranteeing their commitment to human rights at all levels.

References

A/HRC/8/5. Protect, Respect and Remedy: a Framework for Business and Human Rights - Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie. 7 April 2008. (available at http://www.unglobalcompact.org/docs/issues_doc/human_rights/Human_Rights_Working_Group/29Apr08_7_Report_of_SRSG_to_HRC.pdf)

A/HRC/17/31. Guiding Principles on Business and Human Rights: Implementing the United Nations' "Protect, Respect and Remedy" Framework - Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie. 21 March 2011. (available at http://www.ohchr.org/Documents/Issues/Business/A-HRC-17-31_AEV.pdf)

A/HRC/RES/17/4. Human rights and transnational corporations and other business enterprises (available at http://www.unglobalcompact.org/docs/issues_doc/human_rights/A.HRC.17.RES.17.4.pdf)

A/HRC/RES/8/7. Mandate of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises (available at http://ap.ohchr.org/documents/E/HRC/resolutions/A_HRC_RES_8_7.pdf)

AVERY, Christopher, SHORT, Annabel, and REGAIGNON, Gregory Tzeutschler. Why all companies should address human rights – (and how the Business & Human Rights Resource Centre can help). 2005. (available at http://www.cca-institute.org/pdf/avery_business&humanrights.pdf)

CHANDLER, Geoffrey. Commentary on the United States Council for International Business 'Talking Points' on the United Nations Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights. 20 November 2003. (available at http://www.reports-and-materials.org/Chandler-commentary-on-USCIB-Talking-Points.htm)

E/CN.4/Sub.2/2003/12/Rev.2. Norms on the responsibilities of transnational corporations and other business enterprises with regard to human rights. (available at http://www.unhchr.ch/huridocda/huridoca.nsf/(Symbol)/E.CN.4.Sub.2.2003.12.Rev.2.En)

International Centre for Promotion of Enterprises (ICPE). High Level Meeting Press Report, 5 - 6 September 2011, Ljubljana. (available at http://www.icpe.si/high-level-meeting/finall-report)

ROTH, Kenneth. Rules On Corporate Ethics Could Help, Not Hinder, Multinationals. In Financial Times, June 21, 2005. (available at http://hrw.org/english/docs/2005/06/21/global11176.htm)

RUGGIE, John. Introduction by Special Representative, July 2009. (available at http://www.reports-and-materials.org/Ruggie-introduction-to-portal-Jul-2009.doc)

RUGGIE, John. The UN "Protect, Respect and Remedy" Framework for Business and Human Right. June, 2008. (available at http://198.170.85.29/Ruggie-protect-respect-remedy-framework.pdf)

RUGGIE, John. Recommendations on Follow-Up to the Mandate. February, 2011. (available at http://www.business-humanrights.org/media/documents/ruggie/ruggie-special-mandate-follow-up-11-feb-2011.pdf)

United States Council for International Business (USCIB). Talking points on the

Draft "Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with regard to Human Rights" (available at http://www.reports-and-materials.org/USCIB-text-Talking-Points.htm)

Sponsors:

DARS LinkingSlovenia

hse Holding Slovenske elektrarne d.o.o.

Zanesljivo vsepovsod POŠTA SLOVENIJE

VISION OF ICPE

to become a hub of excellence in financial and social responsibility performance for public enterprises; based on its 35 year history and experience as well as on the network of existing and new members, affiliated members and international organizations, ICPE seeks to be an important development partner for effective and productive public sector enterprises.

MISSION OF ICPE

to realize this vision the ICPE will work towards developing partnerships with international organizations and Member States;

to become an important partner for efficient and productive public enterprise management with the participation and interaction of a broad range of involved stakeholders - researchers, entrepreneurs, public authorities and with an emphasis on improving dialogue with the private sector. The instruments for this will be the exchange of best practices among its members and through comparative research studies with the aim of upgrading the proficiency and knowledge of public enterprises regarding innovations, analytical tools and advantages of Information and Communications Technologies.