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Privatization in the Republic of Cape Verde

A Preliminary Assessment

Final Report

March, 1992

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March 5, 1992

Re: Privatization and Development Project (PAD)
Contract No.: DPE-0016-Q-00-1002-00
USAID/Cape Verde - Privatization in the Republic
of Cape Verde - A Preliminary Assessment
PIO/T No.: 655-0015-3-10010

Dear Mr. Goncalves:

We are pleased to present twenty copies of the Final Report of Privatization in the Republic of Cape Verde - A Preliminary Assessment. All comments received on previous drafts have been incorporated into the Final Report.

It has been a pleasure to work with USAID/Cape Verde on this important project. On behalf of Andrew D. Cao, Project Manager, we would like to acknowledge the enthusiastic assistance provided by the staff of OAR/Praia. The International Privatization Group at Price Waterhouse looks forward to working with you again as the Cape Verde privatization program develops.

Sincerely,

Price Waterhouse

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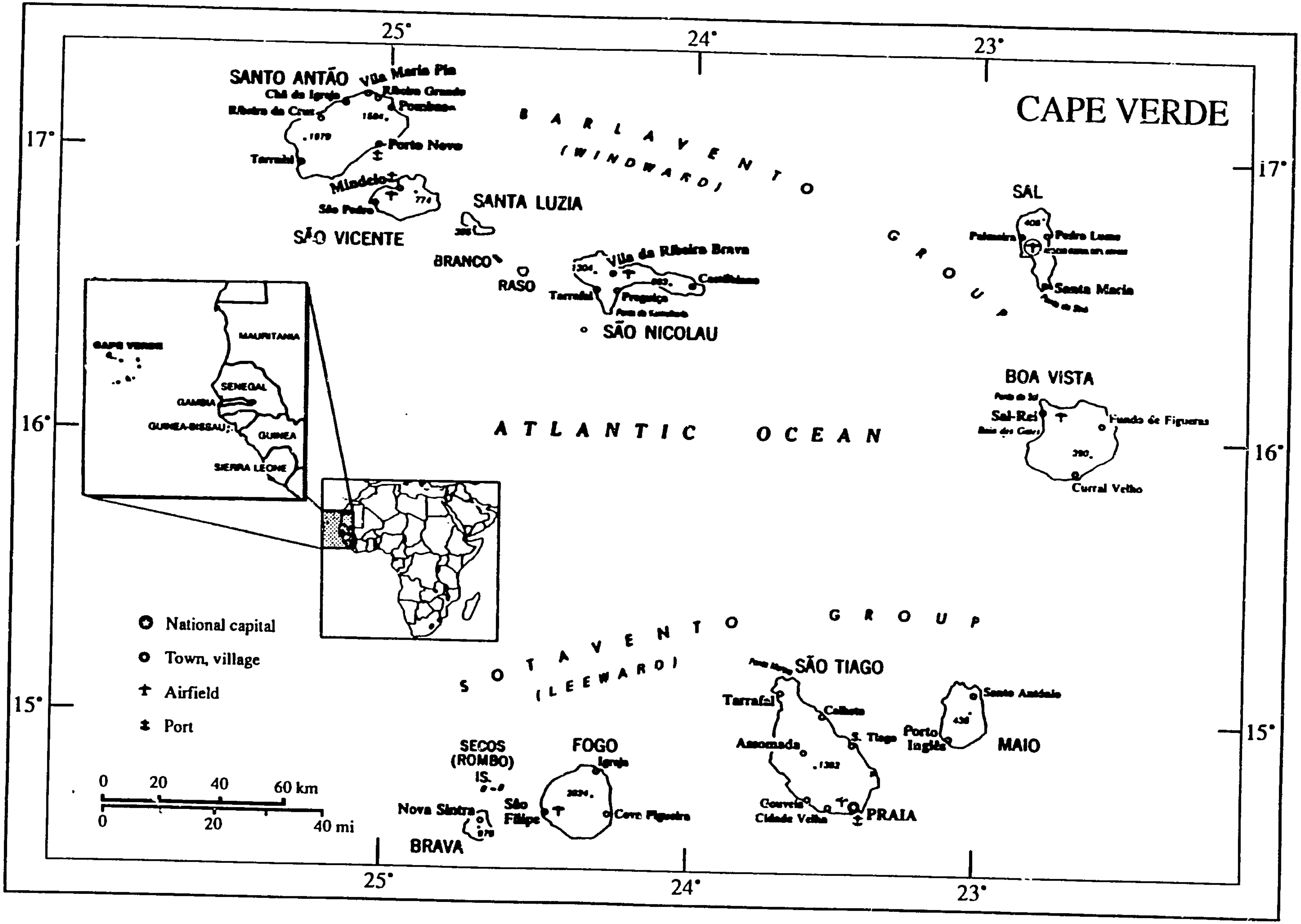
LIST OF ACRONYMS AND NAMES

ADB	African Development Bank
BCV	Bank of Cape Verde
CAAP	Water distributor in Praia
CABETUR	Tourism company
CABNAVE	Ship repair company
CEP	Post office savings bank
CTT	Telecommunications company
CVE	Cape Verde Escudo (CVE67 = US$1, November 1991)
ELECTRA	Electricity and water company
EMPA	Basic food distribution company
EMPROFAC	Pharmaceutical and medical equipment company
ENACOL	National oil company
ENAVI	Poultry and related products company
FAMA	Pasta producing company
FAP	Agricultural products and equipment company
GOCV	Government of Cape Verde
GDP	Gross domestic product
HOTELMAR	Hotel operating company
IMF	International Monetary Fund
INTERBASE	Cold storage plant and international fish marketing company
IPC	Income per capita

MAC	Building construction materials company
MOFP	Ministry of Finance & Planning
MORABEZA	Garment company
MpD	Movimento para a Democracia
PESCAVE	National fishing company
PW/IPG	Price Waterhouse, International Privatization Group
SITA	Paint manufacturing company
SOCAL	Shoe company
SOCAPESCA	Private fishing company
SOE	State-owned enterprise
TACV	National airline company


CAPE VERDE
SANTO ANTÃO
Vila Maria Pia
Ribeira Grande
Ribeira da Cruz
Porto Novo
Tarrafal
Mindelo
São Pedro
SÃO VICENTE
SANTA LUZIA
BRANCO
RASO
Vila da Ribeira Brava
Tarrafal
Preguiça
SÃO NICOLAU
B A R L A V E N T O
(W I N D W A R D)
G R O U P
SAL
Palmeira
Pedra Lume
Santa Maria
BOA VISTA
Sal-Rei
Fundo de Figueras
Curral Velho
MAURITANIA
SENEGAL
GAMBIA
GUINEA-BISSAU
GUINEA
SIERRA LEONE
A T L A N T I C   O C E A N
National capital
Town, village
Airfield
Port
S O T A V E N T O   G R O U P
(L E E W A R D)
SÃO TIAGO
Tarrafal
Calheta
S. Tiago
Assomada
PRAIA
Cidade Velha
Porto Inglês
MAIO
SECOS (ROMBO) IS.
FOGO
Igreja
São Filipe
Nova Sintra
BRAVA
0 20 40 60 km
0 20 40 mi
25°
24°
23°
17°
16°
15°

EXECUTIVE SUMMARY

PURPOSE

The current democratic Government of Cape Verde (GOCV) is committed to the economic liberalization of the country. As is the case with many countries in the world today, the GOCV has identified privatization as an important strategy by which the goals of sustained economic and social development can be achieved.

The purpose of this study is to conduct an assessment of the economic, social and political environment of Cape Verde in order to propose preliminary guidelines for a privatization program.

BACKGROUND

Although the GOCV does not have a privatization plan, it has the political will and commitment necessary to privatize its state-owned enterprises (SOEs). Both the President and the Prime Minister have demonstrated their commitment to the economic liberalization program, of which privatization will become an integral component. The GOCV has also taken steps to restructure its legal system to support these economic initiatives.

FINDINGS

The privatization effort could encounter substantial hurdles related to the labor force and the lack of a developed financial sector. Issues related to the labor force include the shortage of traditional and technical schools, which results in a generally low level of education. This in turn contributes to a high unemployment rate and the inefficiency of the productive sector. Labor redundancy is also a significant issue, as the existing labor laws do not provide proper incentives for increasing productivity. A hurdle also exists in the country's limited financial sector.

Despite a virtual monopoly in most economic sectors which permits many SOEs to have high gross profit margins over time, inefficient management of operating costs, including high wages and salaries due to overemployment, erodes operating profit margins drastically, causing most SOEs to have negative net profit margins.

Overall, wholly-owned SOEs tend to be less efficient than mixed SOEs and private firms appear to be the most efficient among the three groups. All three groups taken as a whole show a general problem of poor management of operating costs in the Cape Verdean market. This can be attributed to the shortage of managerial capability discussed above. The sizable gross profit margins found among all three groups indicate that with proper managerial inputs and competition via privatization, there is a good opportunity for investors and the economy in general to gain from privatization.

RECOMMENDATIONS

The recommendations consist of the systematic steps that need to be taken by the GOCV in order to improve the likelihood of successful privatization and financing alternatives for privatization funding, and a plan of action to be considered by USAID and other donors.

Plan of Action for the GOCV

It is recommended that the GOCV pursue the following principal activities:

- Form a full-time privatization organization reporting directly to the Prime Minister or the Minister of Finance and Planning with representatives from the various ministries, private business associations, labor unions and the media.

- Define and prioritize the objectives of the privatization program. It is recommended that efficiency be established as a long-term objective and accorded the highest priority.

- Formulate a privatization strategy which considers unemployment and other critical issues. It is important for the GOCV to manage these issues from the beginning in order to maintain social and political stability throughout the course of the program.

- The GOCV must begin to explore sources of financing for its privatization program other than the assistance provided by international donor agencies. Alternatives include funding from Cape Verdean emigrants, privatization fund development, commercial papers, convertible preferred stocks and bonds, employee stock ownership plans and venture capital via BOT.

Plan of Action for USAID and other Donors

The following activities are recommended for USAID and other donor assistance:

- Long Term Advisor to assist the GOCV throughout all phases of the program.

- Case Study on the shoe company SOCAL, privatized in 1989. This transaction provides ideal material for examination of lessons learned in terms of privatization policy formulation and strategy design.

- Basic privatization training for practitioners during the first phase of the privatization program. Advanced technical training on privatization subjects such as valuation techniques will be necessary during the second phase.

- Assistance on valuation, negotiation and transfer of ownership during the third phase of implementation.

- Assistance with information dissemination is required throughout the program in the form of public relations and the development of a documentation center where studies on privatization will be stored for consultation.

BACKGROUND OF THE PROJECT

The current democratic Government of Cape Verde (GOCV) was recently overwhelmingly elected on a platform of political and economic liberalization. The GOCV has adopted the principle of equal access to resources, economic competition and private sector development with a limited role for the State in strategic sectors only.

In light of this new development, the Minister of Finance and Planning (MOFP) solicited USAID assistance to undertake a preliminary study on privatization. The purpose of this consultancy, therefore, is to conduct an initial assessment of the environment, and the potential for and limitations to undertaking a privatization program in Cape Verde.

INTRODUCTION

The dominance of the state in various economic sectors of a country dates back to the necessity for control during the colonial period and in countries with socialist or communist economic systems. With the collapse of the socialist system throughout the world, a strong private sector has been recognized as the only way to promulgate free market forces and promote sustained economic and social development. Worldwide, governments realize that they can no longer try to artificially solve the unemployment question by absorbing a growing labor force in state-owned enterprises (SOEs). Faced with unproductive SOEs, a rising subsidy burden, and a high level of unemployment, governments in industrialized countries such as the United States, Great Britain, France, Italy and Germany, and in developing countries such as Chile, Senegal, the Mauritius Island, Jamaica and Malaysia have chosen to privatize their SOEs.

The word "*privatization*" is a new word which was added to the development lexicon in the late 1970s as a new economic development concept. Although the word still conveys many things to different people, it is broadly understood as the transfer of management or ownership of productive activities from government to private hands. The forms of transfer vary and will be discussed in detail in Section III.

The purpose of this study is to assess the economic, social and political environment of Cape Verde in order to propose preliminary guidelines for a privatization program. This study was undertaken between November 16, 1991 and December 12, 1991 by a team of Price Waterhouse consultants. Because of time limitation, a trade-off between scope and depth is inevitable. Further studies recommended in this report need to be started immediately in order to maintain the necessary momentum for successful privatization.

This report consists of three sections. Section I overviews the economic, social and political environment of privatization and Section II analyzes a sample of SOEs. Based on the first two, Section III discusses various steps and options for future follow-up activities.

METHODOLOGY AND LIMITATIONS

Secondary sources of data were collected by the team during the first week in Cape Verde. After an in-depth analysis of the economic, social and political data on the country and of a sample of the public and private firms, interviews were conducted during the following weeks in order to collect data not available through secondary sources.

Personal interviews were used to collect and verify certain data as well as to assess the understanding, perception, attitude, and opinion of various interest groups such as the staff of the ministries, central bank, SOEs, private corporations, and various international donors. The sample of SOEs was selected using a random stratified sampling technique, according to the following criteria: a) on the percentage of state ownership to compare the wholly-owned SOEs to joint ventures and to private firms; and b) on the types of economic activity such as hotel, garments, fishery, telecommunications, sea transportation, airline, food processing, food distribution, paints, electricity and water, pharmaceutical, metal works, construction, and plastic and aluminum production. The sample represents around half of the SOEs in the country.

Wherever possible, three years of financial data is used to smooth cyclical variations. Univariate statistics are computed to measure the typical characteristics as well as variations. This method of data analysis allows a better comparison over time between wholly-owned vs. mixed SOEs and private enterprises. It also will provide for pre-post privatization comparison and, more importantly, control and management of privatization impacts.

The major difficulty encountered during this study was the lack of availability of more current data and audited financial statements, which is a common phenomenon in many countries. For this reason, the analysis is limited to the years for which data is available.

SECTION I

THE ENVIRONMENT FOR PRIVATIZATION IN CAPE VERDE

I. POLITICAL WILL AND COMMITMENT

A strong commitment to economic liberalization has been declared as the platform of the democratically elected President of the Republic of Cape Verde, Dr. Antonio Mascarenhas Monteiro. Privatization has become a crucial element of the national economic reform program, not unlike the cases in Eastern Europe where the question is no longer "why" but "how" to best privatize in order to improve the quality of life for the people.

The Prime Minister, Dr. Carlos Veiga, has also indicated that decentralization is one of his top priorities in order to provide the necessary institutional support for economic liberalization. Although there is no written privatization policy yet, private health care and private education have recently been permitted. The GOCV has already privatized a shoe company, SOCAL, in 1989. Since this is the first assessment for privatization in Cape Verde, no objectives have been established yet. However, the GOCV has indicated that the fisheries and tourism industries are to be developed further because of their potential for growth and their spillover effects into many other areas such as food processing, hotel, construction, transport, telecommunications, water and electricity.

The government is also reforming the legal system in order to bring it more in line with the liberalization program. Among others, the Commercial Code will be overhauled to conform with the establishment of a freer market economy. Additionally, the GOCV will introduce legislation to ensure that Cape Verdean emigrants have the same rights as local residents as well as provide greater investment incentives.

Although the legal framework has not addressed the issue of "strategic" versus "non-strategic" SOEs yet, the political will and commitment to the long term goals of sustained economic and especially social growth will have to consider the political aspects of the strategic problem. This problem includes issues such as social unrest resulting from labor displacement and potential instability of food security by mass privatization or privatization of food related SOEs such as EMPA or the domestic inter-island shipping SOEs. National security is another politically "strategic" area when dealing with telecommunications, transport and banking in countries where there is a fear of foreign control of these industries.

However, lessons learned from other countries indicate that the fear of privatizing the so-called "strategic" SOEs is not well founded politically because the interests of national security can be served through regulation and the risk of social unrest minimized through the selection of appropriate privatization strategies. Furthermore, the perception of what is "strategic" will be covered in interviews with the managers and decision makers in Cape Verde in order to find out whether the concept is actually a real concern of the majority or simply the opinion of a few who may be opposed to the privatization program.

II. AGGREGATE ECONOMIC ENVIRONMENT

Cape Verde is located at the crossroads of three continents, Europe, Africa and Latin America, lying about 500 km from the coast of Senegal in the Atlantic Ocean. As shown on the map, the archipelago is scattered over 58,000 km^2. Due to this geography and a thin domestic market with a population of approximately 356,000, tourism and fisheries constitute the two sectors of the economy with the highest growth potential. However, privatization could also be used as a way to diversify the economy and rebalance its structure by developing other economic sectors. A privatization policy must be part of a well integrated economic development plan with all the linkages between the various sectors clearly identified.

Because Cape Verde does not yet have a privatization policy nor any written strategy, this section on aggregate economic assessment is necessary in order to provide guidance for privatization policy formulation and to establish the foundation for more specific recommendations on the action plan to be discussed in Section III of this report. As the focus is on privatization, the analysis will cover only those variables which have direct implications for privatization.

A. Economic Structure and Performance

1. The First Economic Development Plan (1980-85)

Classified by the World Bank as a middle income country with per capita income of U.S. $680 in 1988, the economic structure of Cape Verde is dominated by the service sector which accounted for around 65% of the total GDP of CVE 19 billion in 1988. The industrial sector accounted for 20%, of which 7% was in manufacturing. The remaining 15% was generated by the agricultural sector. This is an unusual sectoral distribution for a developing country and the implication for the formulation of privatization policy would be to integrate it within the overall economic restructuring policy of the country. In fact, the priority that the GOCV gives to a particular sector in its economic development plan will also influence the SOEs targeted for privatization.

The first economic development plan for 1980-85 set a target of CVE 22.1 billion investment at 1982 prices with a projected GDP growth of 12% annually. However, the realized investment level was only 60% of the projected investment target. Real growth in the productive sectors averaged only 3% annually during the first plan period. The actual number of new jobs created was approximately 3,500 compared to the target of 6,000 and exports reached only U.S. $28 mn in 1985 vs. the planned U.S. $42 mn.

The immediate implication for privatization policy formulation is to evaluate the absorption capacity of the country by sector and between sectors because this will determine the appropriate pace for privatization. Because public administration in Cape Verde is recognized as frugal and efficient by various sources such as the International Monetary Fund (IMF), the African Development Bank (ADB) and the World Bank, the issue of absorption capacity could be attributed more to a fundamental problem of the economic structure rather than due essentially to management, discussed as follows.

2. *The Second Economic Development Plan (1986-90)*

Learning from the experiences of the first plan, the second development plan for 1986-90 projected a total investment of CVE 31.2 billion at 1985 constant prices with an annual growth of government spending of no more than 5% and a projected external source of finance of CVE 28 billion. The plan forecast an average GDP growth rate of 4.5% above the population growth rate of 2% annually. The targeted annual growth rate for agriculture, livestock and forestry was 3.5%, 4.8% for hotel construction and tourism and 5% for fisheries.

3. *Structural Limitations*

a. Education. One fundamental problem which might hamper the absorption capacity of Cape Verde could lie in the limited level of education made available in the country due to inadequate facilities, unqualified teachers, unsuitable curricula and shortage of textbooks and materials. There are only four general secondary schools and one technical school in Cape Verde. In the capital city of Praia, two schools have had to run double shifts, enrolling 4,395 students which constitute 93% of the total number of secondary students. The technical school located in Mindelo, on the island of San Vicente, teaches basic commercial and industrial skills. Because of the shortage of technical skills, firms have had to train their own employees.

The implication for privatization policy formulation is that unless more resources are devoted to technical training, the labor force of Cape Verde will not be able to handle the increase in demand for qualified employees by the expanded private sector and more importantly by the foreign direct investors who would expect some comparable international standard. Without such training efforts, the current unemployment rate of 25% of the total active population of 107,000 will not decline with privatization.

b. Labor Law. In the formulation of the national privatization policy and strategy design, the GOCV needs to address the problem of rigidity found in the current labor law which does not provide the incentive for workers to perform at their optimum efficiency because employers cannot fire for overall poor performance. For this reason, two firms providing the same product such as petroleum could have considerable difference in labor productivity. ENACOL, an SOE which supplies around 30% of the market has a labor force of 125 workers while Shell Cabo Verde, a private firm, holding the remaining 70% of the market, has 75 workers.

Cape Verdeans are known to be industrious people in the US, Europe and other African countries where they have emigrated. With an appropriate labor law, such invaluable human resources could be used to their maximum potentials. In fact, productivity in Mindelo and in Sal is considered to be higher than in Praia because of more competition in the labor market. SOCAL which is a privatized firm with Portuguese and Cape Verdean investors producing shoes, reported that its productivity is close to 75% of the Portuguese level. In EMPA, workers are paid on a piecework basis as provided by the law; however, this practice is not widely used by SOEs. In interviews, all managers indicated that workers respond well to work incentives such as bonuses with higher productivity, better quality and lower absenteeism.

c. Financial Institution. Another structural limitation to be dealt with in the formulation of a privatization policy is the inadequacy of the financial market. Currently, Cape Verde has a unibank structure with the Bank of Cape Verde (BCV) assuming the roles of a commercial bank, a development bank and a central bank. The Post Office Savings Institution (CEP) is a small savings institution which attracts only 1% of total deposits and which makes small loans to civil servants for housing and personal consumption. The loan portfolio of BCV is clearly imbalanced with 10% of total credit allocated to agriculture and fisheries, 30% to industry and the remainder to the service sector.

B. Sectoral Performance

1. Agriculture and Fisheries

The agricultural sector in Cape Verde is very limited because only 10% of the country's area or 37,000 hectares are suitable for cultivation. Furthermore, excessive droughts have regularly affected agriculture on the islands. The last severe drought lasted for more than fifteen years causing large waves of emigrants to the US, Europe and other African countries.

In terms of fisheries, there are about 1,200 boats of four to six meters in the artisanal fishing sector, supplying mostly the domestic market with a total productivity of around 10,900 tons per year, half of which is tuna. The fishing potential has been estimated at 35,000 to 45,000 tons per year. Beside tuna, the catches include yellowfin, grouper, snapper, barracuda, and lobsters -- all of which represent a high potential for export. Currently, fish exports constitute 70% of total exports.

If the development of the fishing sector is a priority of the GOCV, the formulation of a privatization policy should examine Interbase and Pescave. Interbase is a state-owned fish marketing company with cold storage facilities and a block ice factory. Pescave is the national fishing company with a fleet of 11 vessels. Any privatization policy should not only look into one single economic sector, but also needs to consider the linkages that occur between adjoining economic sectors. In the case of Cape Verde's fishing sector, the seaport and sea transportation sectors are closely inter-linked and should thus be examined as well.

2. Industry

According to a 1992 UNIDO Survey, the industrial sector in Cape Verde consists of around 534 manufacturing enterprises and experienced an average annual growth rate of 3% in the 1980s. (This figure excludes family businesses producing furniture and bread.) The manufacturing sector has become well-established after independence in 1975 and has focused on the domestic market with the assistance of a government import-substitution policy. Currently, no data is available to determine the cause of low capacity utilization in Cape Verde which varies between 25% and 40% among the firms. Possible explanations, as indicated in the interviews, of such low capacity utilization could include: the small domestic market, the inefficiencies of SOEs, and the inappropriate capital intensiveness of technology.

The implication for privatization policy formulation and strategy design is that efficiency improvement must be one of the most important objectives of the GOCV. Higher capacity utilization tends to reduce unit cost of production, giving the firm a higher and wider margin for pricing variation to stimulate demand which is mostly elastic in Cape Verde. With appropriate marketing, total revenue and total profit could increase even with lower prices due to the high elasticity of demand.

If the GOCV decides that efficiency is one of the major objectives in the privatization policy, and if it is actually realized in the implementation stage through appropriate management of the privatization process, then the current imbalance in the economic structure of the country would be immediately alleviated because of the greater contribution put forth by the industrial sector. It is not inconceivable to expect that those firms which have been operating at 25% capacity utilization as an SOE could be improved to 50% or even 75% in the private sector over the next few years. Such higher capacity utilization coupled with competitive pricing could make Cape Verdean manufactured goods more attractive in the international markets as well. Privatization would therefore help redirect the industrial sector toward exports, hence providing greater opportunities and larger markets.

Currently, the industrial sector employs around 3,000 people, which accounts for approximately 3% of the country's labor force, half of whom are employed by SOEs. Only one firm employs more than 200 people (CABNAVE); three employ between 100 to 200; six employ between 50 to 100 and the rest are small firms employing less than 50 people. The smaller firms are mostly bakeries, rum distilleries and furniture manufacturing. Since a higher capacity utilization will increase demand for skilled labor, a formulation of a Cape Verdean privatization policy has to consider training programs and financing options.

3. Tourism

Tourism accounts for 2% of GDP with around 20,000 visitors per year. The Hotelmar Corporation (Sociedade Hoteleira de Cabo Verde) runs the country's hotel chain which consists of one four-star hotel in Praia and one two-star hotel in Fogo.

Because tourism covers airlines, airports and infrastructure services such as water, electricity, telecommunications and sewage systems, privatization policy formulation needs to consider all these interrelated sectors as a whole rather than just the sum of the parts for proper coordination and logical development during the various phases of privatization. One example of careful planning would be considering the impact of a new international airport in Praia on the existing airport in Sal, on the fleet of airplanes run by TACV, and on hotel development plans in Sal and in Praia.

4. Electricity, Water and Telecommunications

a. Electricity. Virtually all electricity generation is performed by diesel generators run by ELECTRA which should provide adequate capacity for both the short and medium term in Praia, Mindelo and Sal. Blackouts are not common and back-up generators are therefore not a standard practice for industries. The cost of electricity for industrial users is computed based on a six-part formula and varies with each firm. SOCAL reports that its electricity cost is CVE 14/kwh or around US$0.19/kwh which is above an average cost of US$0.09/kwh for comparable large diesel generators. In Costa Rica the cost is US$0.03/kwh and US$0.25/kwh in Senegal.

In Praia, ELECTRA is in the process of installing two new generators of 3MW each in addition to the 4.2MW supplied by the existing generators. Currently, the maximum demand is only 3.3 MW. In Mindelo, peak usage is 3.4 MW and the current supply consists of two generators with a combined capacity of 4.4 MW plus two older secondary generators of 1 MW each. In addition, there is 300kw capacity from wind generation. In Sal, the maximum demand is 1 MW and the maximum capacity available is 1.75 MW and there are plans to install another 1 MW generator. Cape Verde should be able to supply adequate power to cover demand until at least 1995, which implies that this sector is not an immediate priority in the privatization policy formulation.

b. Water. Water distribution is handled primarily by two SOEs: Mindelo's and Sal's by ELECTRA, and Praia's by CAAP. While Praia relies on groundwater, both Mindelo and Sal use desalinated water. The shortage of water constitutes a serious problem. In Mindelo for example, the daily demand is estimated at 3,000 m^3 while the supply is 1,900 m^3 per day. The water tanks of residences and industries are supplied once a week only. In Praia, the supply is estimated at 2,100 m^3/day compared to a demand of 3,000 m^3/day, which has led to water rationing in various parts of the city.

The production cost for desalinated water, excluding distribution costs, is CVE 180/m^3 in contrast with CVE 40/m^3 for groundwater. Meanwhile, the rate for industrial users is set at CVE 160/m^3 or US$2.19/$m^3$ compared to US$0.25/$m^3$ in the Dominican Republic or US$0.67/$m^3$ in Togo. The privatization policy formulation has to include water because of the welfare of the people as well as its impacts on the production costs of all economic activities in the country.

c. Telecommunications. CTT handles the postal services and telecommunications. Overall, the quality of service is average to poor for both domestic and international. There is a long waiting list for new telephone hookups and the maximum delay could go up to one year. Currently, direct dialing is only possible to six countries, which are the US, Portugal, France, Holland, Senegal and Angola. International service is provided by a submarine cable and an

INTELSAT Standard B satellite earth station. The submarine cable is scheduled to go out of service by 1993, at which time demand requires that the number of circuits be tripled.

Telephone cost per minute from Cape Verde to Portugal is CVE 140/min. or US$1.92/min. compared to the same corresponding call from Mauritius to France or from Kenya to the UK of between US$1.60 to US$1.69 per minute. The significance for a privatization policy formulation is to incorporate plans for expansion of the telecommunications sector in conjunction with the related industrial and tourism sectors.

5. Transportation

Because of the distances between the islands, sea and air modes of transportation constitute one of the most strategic sectors of the economy as they affect exports, tourism, food and raw material distribution.

a. Sea Freight. Service is infrequent with only two to three ships per month to Europe compared to nine per month from Mauritius and daily service in Costa Rica. The sea freight rate from Cape Verde to Europe is around US$1,900 per 20 foot container, nearly twice the rate charged in Togo or Honduras for the same distance. The irregularity and the cost of sea freight have often caused SOCAL and MORABEZA to rely on air freight to meet delivery deadlines.

The two principal ports of Mindelo and Praia are not well configured for container handling. Neither port has a specialized container crane to handle container weight above 12 tons, yet the typical full container weighs 20 tons. Handling cost is charged by the hour rather than by the ton and it is therefore comparatively higher than in other ports. Unloading a container may sometimes take up to one hour, while with proper equipment, other African countries can unload eight to nine containers per hour. Last but not least, both ports lack storage space area. Mindelo for example has only space for 100 containers.

b. Air Transportation. Service is provided by TACV with only two flights per week to Portugal compared to several daily international flights from the Caribbean countries. Air freight from Cape Verde to Europe is expensive with US$1.90 per kg from Mindelo or Praia to Portugal compared to US$1.72/kg from Mauritius or US$1.56/kg. from Togo. The planes used for domestic air transportation between the islands constitute a serious problem because of limited cargo space. Tourists often wait one or more days to get their luggage because of the small cargo size of the planes. The problem is aggravated by TACV's inability to maintain published schedules.

Obviously, air transportation must be an integral part of the privatization policy formulation as it impacts on so many other economic sectors. This will be particularly important with the future plans of the airport expansion in Praia because the expansion's net impact on the overall economy has to be evaluated carefully.

C. Strategic in Economic Terms

From the economic standpoint, both aggregate performance and sectoral performance of the country has been weak. It is therefore imperative to rely on a new approach such as privatization to improve the economic outlook. Strategically speaking, without the adoption of this new approach, the country cannot achieve self-sustenance, and will remain dependent upon external assistance, an option which is not economically viable in the long run. Economically speaking, no SOE should be considered non-privatizable. In fact, food security can be a counter-argument to those who object to privatization using the strategic argument because with privatization, more efficient production, distribution and pricing of goods accompanied by efficient regulation will contribute to the general welfare. This fact has been proven to be true in Taiwan, Hong Kong and Korea. The same rationale can be applied to other sectors such as transportation, telecommunications, and particularly banking.

SECTION II

ASSESSMENT OF STATE-OWNED ENTERPRISE PERFORMANCE

I. PERFORMANCE INDICATORS

In assessing the performance of the SOEs, universal measurement standards are used for conformity and consistency. The vital signs of the SOEs analyzed in this preliminary assessment prior to privatization could be compared later to the same performance indicators post-privatization. Without these indicators, post-privatization monitoring and impact management cannot be made for each period following the privatization transaction in order to adjust for successful implementation.

The vital signs consist of the liquidity of the SOEs which measures the ability of the firms to meet their current liabilities; the efficiency in the management of their investment in assets in order to generate revenue; the risk to which they have exposed the firm by relying on debt financing and the resulting profitability for the firms.

The indicator used to measure *liquidity* consists of the "current ratio" (CR) of the SOEs which compares how much current assets such as cash are currently available to pay the current obligations of the firm. A ratio of one or higher means that the firms are liquid with low risk of forced bankruptcy due to the inability to pay current debt. Typically, SOEs tend to be mostly illiquid because they tend to count on the government to bail them out in case of difficulty.

To measure *efficiency* in asset management, the most aggregate indicator used is the ratio of total sales divided by total assets called "total asset turnover ratio" (TATO). An SOE with a TATO of 8 is more efficient than another SOE with a TATO of 2 because while the former generates sales of CVE 8 for each escudo invested in total assets, the latter achieves four times less, generating only sales of CVE 2 per escudo invested in total assets.

Efficiency in asset management can also be measured specifically for each type of asset. The "fixed asset turnover ratio" (FATO) which equals to sales divided by fixed assets measures how much sale each escudo invested in fixed assets such as plants, building and machinery generates. This is particularly important in the case of Cape Verde because of its small market size. Since machinery and equipment used by certain SOEs were donated in-kind by other countries, there is no control over the size nor appropriateness of the level of technology. This will partially explain why there is such a low level of capacity utilization in so many SOEs. The FATO also gives some indication about the efficiency in the production department of the firm which utilizes the assets. Efficient production tends to make higher quality products which attract more sales. Efficient production also tends to lower unit fixed cost with high capacity utilization allowing the firm to price the product at a more competitive level.

9A

TABLE 1A

ANALYTICAL MATRIX OF DEPARTMENTAL EFFICIENCY

Income Statement	Responsible Department	Profitability Ratios
Total Revenues (TR)	**Marketing**	
− Cost of Goods Sold	**Production**	
= **Gross Profit** (GP)		**Gross Profit Margin (GPM)** **GPM= GP/TR**
− Operating Expenses	**General Administration**	
= **Earnings Before Interest and Taxes** (EBIT)		**Operating Profit Margin (OPM)** **OPM=EBIT/TR**
− Taxes	**Finance**	
− Interest		
= **Net Profit** (NP)		**Net Profit Margin (NPM)** **NPM= NP/TR**

TABLE 1B

ANALYTICAL MATRIX OF DEPARTMENTAL EFFICIENCY

Balance Sheet	Responsible Department	Measurement Ratios
Assets		**Liquidity**
Cash & Equivalents	**Finance**	Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$
+ Accounts Receivable	**Finance & Marketing**	**Efficiency** Days Sales Outstanding = $\frac{\text{Acct.s Receivable}}{\text{Sales/360}}$
+ Inventory = **Current Assets** + Fixed & Other Assets = **Total Assets**	**Finance & Production**	Inventory Turnover = $\frac{\text{Sales}}{\text{Inventory}}$ Fixed Asset Turnover (FATO) = $\frac{\text{Sales}}{\text{Fixed Assets}}$ Total Asset Turnover (TATO) = $\frac{\text{Sales}}{\text{Total Assets}}$
Liabilities		
+ Current Liabilities + Medium & Long Term Liabilities	**Finance**	Notes Payable Outstanding (NPO) = $\frac{\text{Long Term Liab.s}}{\text{Sales/ 360}}$
= **Total Liabilities**	**Finance**	Debt to Total Assets = $\frac{\text{Total Debt}}{\text{Total Assets}}$
+ Owners' Equity	**Finance**	**Profitability** Return on Equity (ROE) = $\frac{\text{Net Income}}{\text{Owners' Equity}}$
= **Total Liabilities & Equity**		

Another efficiency indicator measures the ability of the firm to collect its credit sale on time and is called the "days of sale outstanding ratio" (DOSO). While credit sale is necessary as a marketing tool, inefficient collection reduces the amount of cash made available to the firm to cover its operations, and hence, its liquidity is jeopardized. Furthermore, SOEs with poor collection of credit sales tend to be unable to pay their suppliers who also have sold them on credit, leading to a high "notes payable outstanding ratio" (NPO). This chain effect is detrimental to the business development of Cape Verde. With a private firm, managers try to collect faster because it is "our" money.

In terms of *profitability*, different indicators are used to pinpoint the contribution of different departments within the firm. The most aggregate profitability ratio is the "return on total asset" (ROA) which is often referred to as the "return on investment" (ROI) as well. It is equal to the net income divided by total assets. For private owners, the relevant ratio is the "return on equity ratio" (ROE) because they want to know how much profit they have made for each dollar they have invested. This ROE ratio will become very important during the privatization transaction phase because investors might decide to invest in one privatized SOE instead of another because of this guiding selection criteria. The ROE ratio could also serve as a basis for the GOCV to compute the discount rate in valuating the SOEs for sale.

The "gross profit margin ratio" (GPM) measures the efficiency of the marketing and production departments and is equal to gross profit divided by sales. To measure the profitability contribution of the general administration of the firm in terms of administrative expenses such as salaries, wages or office expenses, the "operating profit margin ratio" (OPM) is derived, which equals the operating profit before taxes and interest (EBIT) divided by sales.

Leverage measures how much debt is used to finance the firm beside money from equity by calculating the "debt to total asset ratio" (DR). Finally, the "times-interest earned ratio" (TIE) measures the ability of the firm to pay its interest obligations and is equal to the EBIT divided by total interest expenses.

For each SOE, the above indicators are computed for each of the last three years. The mean average is calculated to measure the typical characteristic in order to reduce possible biases caused by cyclical variations which often exist from one year to the next. To check the reliability of the mean average, the standard deviation is computed for each ratio as well. High standard deviations indicate high variation and the mean average should be interpreted with some reservation. The means and standard deviations are presented in the summary table while the individual tables for each of the firms as well as their consolidated financial statements are provided in the Appendix section. Finally, a preliminary attempt is made to compare the mean performance between wholly-owned SOEs vs. partially-owned SOEs vs. private firms as three groups to detect performance differences using cross-tabulation.

There are currently 19 wholly-owned SOEs and 14 mixed enterprises in Cape Verde, which account for about 25% of GDP. They cover all kinds of activities, the majority being in the

TABLE II

SUMMARY PERFORMANCE OF ENTERPRISES IN CAPE VERDE

		MEAN			MARKET		RANGE	
		Wholly-Owned*	Mixed*	Private*	Mean	Std. Error	High	Low
LIQUIDITY:								
Current ratio (X)	Current A/Cur. L	1.96	1.24	1.82	167.5%	0.31	1.99	1.36
ASSET MANAGEMENT AND EFFICIENCY:								
Inventory turnover (X)	Sales/inventory	10.60	7.05	3.01	8.89	5.70	14.58	3.19
Days sales outstanding (days)	Receivables/ Sales/360	292.66	119.64	118.66	173.99	81.60	258.78	96.19
Net purchases outstanding (days)	Payables/Cost of Goods Sold/360	926.16	271.20	106.33	435.23	354.99	790.22	80.24
Fixed asset turnover (X)	Sales/Fixed Assets	2.71	5.47	3.99	4.06	1.13	5.19	2.93
Total asset turnover (X)	Sales/Total Assets	0.74	0.48	0.97	0.73	0.20	0.93	0.52
DEBT MANAGEMENT:								
Debt to total assets	Total Debt/Total Assets	51.1%	77.8%	70.4%	66.4%	11.3%	77.66%	55.15%
Times interest earned	EBIT/Interest Expense	20.56	31.28	600.81	217.55	271.04	435.59	-53.50
PROFITABILITY:								
Gross margin	Gross Profit/Sales	56.7%	67.7%	44.1%	56.2%	9.6%	65.8%	46.5%
Operating margin	EBIT/Sales	-15.0%	3.2%	2.7%	-3.0%	8.6%	5.4%	-11.5%
Net profit margin	Net Income/Sales	-20.2%	-10.0%	-7.5%	-12.6%	5.5%	-7.1%	-18.0%
Accounting return on assets (ROA)	Net Income/Total Assets	-3.7%	-2.6%	-4.7%	-3.7%	0.9%	-2.8%	-4.6%
Cash ROA	Net Cash Flow/Total Assets	2.6%	2.1%	0.7%	1.8%	0.9%	2.7%	1.0%
Accounting return on equity (ROE)	Net Income/Total Equity	-89.4%	-40.2%	13.6%	-31.9%	34.5%	2.5%	-66.4%
Cash ROE	Net Cash Flow/Total Equity	-32.5%	25.7%	25.9%	6.4%	27.5%	33.8%	-21.1%

* Annual averages over 3 years (for more details see annex #1)

@ Data includes audited and unaudited financial statements.

\# Only one year of data available.

** Travel agencies have little inventory, so ratio is not meaningful and is excluded from group calculations.

\#\# Both equity and net income are negative, so numbers are not meaningful and are excluded from the group calculations.

@@ CTT has such a low cost of goods sold (99% gross margin) that the net purchases outstanding is not a meaningful ratio.

service area. Currently no data is available to measure the market share of each but from interviews; however, the SOEs virtually have the monopoly in the market.

II. ACCOUNTING ISSUES

Often, the accuracy of the accounting system in a country has been blamed as the major cause for lack of reliability and Cape Verde is no exception. In the context of privatization, reliable accounting procedures and application are vital because they create and maintain the trust of the investors.

Most of the financial statements used in this preliminary assessment are unaudited and, therefore, are not necessarily accurate. Audited financial statements will be needed during the implementation of the privatization transaction and adjustments will be necessary during the valuation process. Until then, financial performance analysis can still be conducted using the above measurements.

Despite the lack of more reliable information, it is still appropriate at this stage to provide the GOCV with an overall picture of the situation based on a rigorous methodology for all SOEs. The rationale is that even in countries where accounting is a well-practiced science the accounting principles are still only generally accepted rather than rules to be followed strictly and, hence, there is always some room for variations.

III. STATE-OWNED ENTERPRISES PERFORMANCE

A. Overall Performance

Overall, despite the virtual monopoly in most sectors which permitted the SOEs to have high revenues and high average gross profit margins (GPM) of 56.7 % for the wholly-owned SOEs and 67.7% for the mixed SOEs as shown on the Summary Performance Table, both groups had negative net profit margins (NPM) of -20.2% and -10%, respectively, because of various inefficiencies explained as follows.

For the wholly-owned SOEs, the drastic drop of GPM from 56.7% to -15% in operating profit margin (OPM) could be explained by the inefficiency in managing operating expenses which include salaries, wages, as well as other administrative costs. This finding which confirms the problem of labor redundancy plaguing the profitability of all SOEs. The same phenomenon existed among the mixed SOEs, although it appears a little less serious than with the wholly-owned SOEs because their OPM still remained positive with 3.2%.

Inefficiency is also found in financial management although the problem is much less serious because the decrease of the OPM was only from -15% to -20.2% in net profit margins (NPM) for the wholly-owned SOEs. For the mixed SOEs, the drop was higher, going from 3.2% OPM to -10% in NPM. The higher reliance on debt financing, as shown by a higher debt ratio (DR) of 77.8% vs 51.1% only for the wholly-owned SOEs, results in higher interest expenses deducted from the OPM. On the other hand, due to the mixed SOEs' reliance on higher financial leverage, their cash rate of return on equity ($ROE) was much higher with 25.7% vs. -32.5% for the wholly-owned SOEs despite their comparable cash rates of return on total asset of 2.1% for the mixed and 2.8% for the wholly-owned SOEs.

Based on the above in-depth analysis of the facts, it appears that mixed SOEs are more efficient than wholly-owned SOEs in most areas of management. As a matter of fact, the mixed SOEs have much better cash flows (which is the true measurement of efficiency because all non-cash expenses have been excluded) despite comparable accounting rates of return because of better tax shield management. Furthermore, as shown on the Summary Performance Table, mixed SOEs were more aggressive in their liquidity management with less idle cash and hence a smaller average current ratio of 1.24 vs 2.04 for the wholly-owned SOEs. Better cash flow management in mixed SOEs also resulted from the faster collection of credit sales of 119.64 days sales outstanding vs. 292.66 for the wholly-owned SOEs. Better collection resulting in higher liquidity available for disbursement explained the faster payments for purchases from suppliers of 271.2 days vs. 928.16 for the wholly-owned SOEs. Mixed SOEs also had higher capacity utilization of their fixed assets which include plants and equipments as shown by their average fixed asset turnover ratio (FATO) of 5.47 vs 2.71 for the wholly-owned SOEs.

Comparing the performance of wholly-owned SOEs with the performance of a small sample of private firms of which data was made available, leads to a similar conclusion, where the same pattern of better summary performance of private firms over wholly-owned SOEs has been found. This can be traced to higher efficiency in all areas of management. Private firms tend to have a less serious problem in terms of operating profit margin, better cashflow management and capacity utilization. They also rely more on debt financing yielding higher cash rates of return on equity.

Because the sample of SOEs used in this study covers around half of the SOE population and represents the major economic activities of most sectors in Cape Verde, a market index which includes some major private firms has been developed just for reference purpose in this Preliminary Assessment. (For further study where more time is allowed, a more comprehensive sample is needed and the market index might be weighted by sales or by assets.) For each ratio, a range around the average has been computed. The "high" end of the range equals the mean plus one standard deviation and the "low" value equals the mean minus one standard deviation. These values were used as market standards for comparison purposes. For example, based on the data shown on the Summary Performance Table, one can conclude that wholly-owned SOEs were less profitable than the "market" as a whole because most of their profitability ratios were lower than the market's. This is caused by less efficient liquidity management and lower capacity utilization as indicated by higher account receivable turnover ratios (close to the high end of the market range indicating lack of aggressiveness) and a lower fixed asset turnover ratio (closer to the low end of the market range).

The market index is also useful in terms of assessing overall prospects in Cape Verde for potential investors. As shown on the Summary Performance Table, the "market gross profit margin" displays a positive 66.4% while the "market operating margin" was only -3% and the "market net profit margin" was -12.6%. Based on these preliminary market indices, it is reasonable to say that the prospect for investors wanting to participate in the privatized SOEs of Cape Verde would be quite good if more efficient management is used. The high gross profit margins imply high market demand and manageable costs of production despite a small domestic market and the need for sizable imports of production inputs. The major problem seems to come from labor redundancy, rather than from the intrinsic attitude of the labor force toward hard work. As a matter of fact, Cape Verdeans in the country and especially emigrants overseas have the reputation and have demonstrated that in the proper environment, their performance is competitive with international standards. The implication for the investor is that the labor issue can be overcome with appropriate management, as both Shell and SOCAL have proven.

(The following section will provide a brief overview of each SOE and an assessment of its privatization prospects. For a more detailed analysis of SOE performance, please refer to the Appendix.)

B. Prospects for Wholly-Owned State Enterprises

1. ARCA VERDE

Companhia Nacional de Navegação Arca Verde, E.P., the national marine transport company, was founded in April 1978 to transport passengers and freight domestically and to transport freight internationally. Legally, the company is organized as a wholly state-owned enterprise (SOE) reporting to the Secretary of State for the Merchant Marine. Its fleet consists of eight cargo ships and ferry boats which are approximately 50 percent depreciated.

Since the domestic transportation of food between islands is considered strategic by only a minority, the GOCV can consider retaining inter-island freight operations, at least until the private sector is able to meet the demand. In the short-term, a management contract could be studied as a means to improve Arca Verde's domestic operating efficiency without compromising its strategic element. As the international freight is neither competitive nor strategic, outright liquidation should be considered. In any case, a feasibility study needs to be undertaken to analyze the potential impact and alternative management requirements of each option.

2. CTT

Empresa Pública dos Correios e Telecomunicações (CTT), based in Praia, was formed in July 1981 to provide postal and telecommunications services for the country, and it currently holds the national monopoly for those services. The company derives 90-95 percent of its revenues from telephone, telex, and other telecommunications services. Postal services comprise the remainder of revenues.

Telecommunications is considered to be a strategic industry by only a few SOE General Managers in Cape Verde. Telecommunications services are especially important to an island nation, but are also an important source of hard currency for the GOCV, generating an estimated $US 500 thousand annually. Given this situation, the GOCV may want to consider the build-operate-transfer method with foreign suppliers for new telecommunications facilities. This option would bring in technology and know-how, while allowing the GOCV to regulate telecommunications and own the system. Another privatization option to be explored is a management contract with a foreign telecommunications firm. This option also allows the GOCV to improve the operating efficiency of CTT and simultaneously to obtain know-how and technology. All options should be carefully studied to determine their feasibility and to select the most beneficial option for the country.

3. ELECTRA

Empresa Pública de Electricidade e Água, Electra - E.P., was formed in April 1982. Electra supplies electricity in Cape Verde; it also supplies water in Mindelo and Sal. The company is wholly-owned by the Government of Cape Verde.

Water and electric services are considered strategic for the development of Cape Verde by a minority of SOE General Managers. If retention of ownership is deemed desirable by the GOCV, build, operate and transfer agreements or management contracts could be used to improve Electra's operations and obtain technological and managerial know-how. Such arrangements would allow the GOCV to enjoy some of the benefits of outright privatization without sacrificing ownership of strategic assets.

4. EMPA

Empresa Pública de Abastecimento, E.P., EMPA was founded in September 1975 as an importer and distributor of essential goods for Cape Verde. The company, which is based in Praia, is wholly owned by the Government of Cape Verde.

EMPA could be considered a strategic company because of its role in guaranteeing food supplies for Cape Verde. Consequently, complete privatization is not a recommended course of action. However, disaggregation of EMPA's businesses into "strategic" and "non-strategic" operations might allow privatization of parts of the enterprise. Basic food distribution is considered strategic and should not be privatized in the foreseeable future. Possible segments of EMPA's operations which may be candidates for privatization are trucking operations, security services, and the inspection department. Privatization of EMPA should be carefully studied to identify the best course of action.

5. EMPROFAC

Empresa Nacional de Productos Farmacêuticos, E.P., known as Emprofac, was founded in June 1979 to import, produce, and sell pharmaceutical products and medical equipment. The company's original mission was to ensure that Cape Verde had a regular supply of medicine at reasonable prices and to promote import substitution through local production. In 1982, the GOCV nationalized pharmaceutical imports. As a result, Emprofac currently has a monopoly on the pharmaceutical supply market in Cape Verde. The company is wholly-owned by the Government of Cape Verde.

The pharmaceutical industry is considered strategic by several Cape Verdeans because of the need to guarantee medical supplies for the country. The strategic designation need not preclude privatization however. Inpharma, which is slated to begin pharmaceutical production in 1992, is a private company and needs to be taken into consideration when evaluating privatization. Emprofac could retain its ownership of Inpharma and Inpharma could start its operations. A part of Emprofac could be sold to private investors. To alleviate concerns about supply of pharmaceuticals, the GOCV could retain a significant ownership of Emprofac. Another option to be evaluated is a merger of the two firms in which the GOCV could retain partial ownership for strategic reasons. All options should be studied carefully in order to select the best course of action.

6. ENACOL

Empresa Nacional de Combustíveis, E.P., Enacol, wholly-owned by the government, is the national oil company of Cape Verde. Enacol, which is based in Mindelo, was founded in December 1979 to import and distribute petroleum products. The team did not meet with Enacol management during its visit to Cape Verde, so this analysis is based on financial statements and secondary sources of information.

Enacol is in a difficult financial situation because it has a negative cash flow. As a result, the company has been borrowing money from the Bank of Cape Verde to cover its shortfall. These funds are unavailable for other uses, crowding out other borrowers in the market, since the GOCV is prevented from advancing other social goals. As a result, the Government of Cape Verde should consider a management contract or a joint venture to turn around Enacol's operations. The GOCV may also want to consider training to prepare Enacol workers for other jobs, as the firm will need to reduce staff to improve its efficiency.

7. ENAVI

Enavi, Empresa Nacional de Avicultura, E.P. was founded in April 1979 to produce and commercialize poultry and related products. Enavi, which is based in Praia, is wholly owned by the Government of Cape Verde. The firm also has operations in Saõ Vicente.

Enavi's business could be divided into two parts: reproduction/supply and production. Because there are currently no competitors in the reproduction/supply market, Enavi fills an important role in the market. This portion of Enavi's business is therefore not a candidate for privatization at present. The production business ultimately could be privatized. Privatization options for the production part of the firm include management buyout, an employee stock ownership plan, or sale of shares in the company. However, prior to privatization the GOCV should consider encouraging competition in the industry, perhaps through gradual price liberalization and incentives to encourage private sector investment. The purpose of fostering competition is to increase supply which would hold prices down.

8. FAP

Fomento Agro-Pecuário, E.P., FAP, was formed in May 1979 to foster agricultural and livestock production in Cape Verde, including the production of animal ration. FAP, an enterprise wholly-owned by the Government of Cape Verde, is based in Praia.

Fomento Agro-Pecuário, because of its support of food production, is considered to be in a strategic industry by some Cape Verdeans. As a result, the GOCV may not consider FAP to be a candidate for sale, but the enterprise must be attended to, as it is making losses. One option for the GOCV to consider would be to split the company into several businesses, each with a clear business focus. For example, animal feed, medicines, and related products could be grouped together. Management contracts or joint ventures might be explored as options to improve the operating efficiency of the new firms. A feasibility study would be advisable to select the best course of action.

9. INTERBASE

Interbase - Empresa de Comercialização de Produtos do Mar, E.P. was established in March 1987 to commercialize seafood. The company is the successor to the former Interbase which combined both fishing and distribution of seafood. Interbase's principal offices are in Mindelo.

Fishing is considered a strategic industry by several Cape Verdeans, and has been targeted for economic development in Cape Verde. Interbase has fine installations which could play an important role in the development of fisheries, especially if the operating efficiency of the company can be improved. Therefore, a joint venture or management contract could be explored as first steps toward eventual privatization. A feasibility study should be conducted to determine the appropriate steps to take.

10. PESCAVE

Pescave, Empresa Caboverdeana de Pescas, E.P., the national fishing company, was also formed in March 1987 after the former Interbase was split into two companies, separating the capture of fish from the commercialization of seafood. Pescave, which is located in Mindelo, is wholly-owned by the Government of Cape Verde.

Under current conditions and in its present form, Pescave would not be a viable candidate for privatization. Fishing has been declared a strategic sector for economic development by the Cape Verdean Government. However, given the company's condition, the health of this industry may be improved by dismantling the business and selling its assets. While private fishermen might be interested in acquiring the fishing boats, price would be an important factor in the sale because of the relative inefficiency of the boats. Another option might be a joint venture with a private investor. In any case, a complete valuation of the company is needed to determine Pescave's worth and to identify the appropriate course of action.

11. MAC

MAC was established in August 1978 to produce building materials. The firm is wholly-owned by the GOCV and is based in Praia. MAC also owns 51.0 percent of MACSOBIL, a glass cutting firm. In January 1992, MAC plans a joint venture to produce reinforced piles and cement products. MAC plans to own 30.0 percent of this new company.

The construction industry is not strategic for the GOCV, so it is not necessary to retain ownership of MAC. The hydraulic cement business has attracted some outside interest. As a result, a joint venture or sale to private investors are privatization options. Employees and management have also expressed interest in buying all or part of the company. In conjunction with privatization, the GOCV should consider retraining of workers, as the firm will need to reduce staff. A feasibility study should be conducted to evaluate the options and determine the best course of action.

12. TACV

TACV-Transportes Aéreos de Cabo Verde, E.P., the national airline, is wholly-owned by the Government. TACV, which is based in Praia, was formed in November 1981 as the successor to the previous national airline company.

TACV needs to improve its operations as soon as possible to relieve the strain on the national treasury. In its current condition, TACV is not a viable candidate for privatization. One option for the GOCV to consider is a management contract to turn around TACV's business. Such a contract would also allow the GOCV to assess the potential impact of the new international airport in Praia on TACV. During the contract, retraining of workers would take place. Ultimately, TACV might be sold to private investors or to a joint venture.

C. Prospects for Mixed Enterprises

1. CABETUR

Cabetur, Sociedade Caboverdeana de Turismo, S.A.R.L., is a travel agency, established in March 1986. The GOCV owns 30 percent of Cabetur, 15 percent through direct ownership of shares and 15 percent through Agência Nacional de Viagens (ANV), another wholly-owned SOE. The remaining 70 percent of the company is owned by private investors, including company employees.

Since Cabetur is not in an industry considered strategic in Cape Verde, many options are available for complete privatization of this enterprise. The GOCV should consider selling its shares, whether by public auction or tender offer. Cabetur employees and management might be interested in acquiring additional shares, as might other private investors. The proceeds from this sale could be directed to fund other privatization efforts such as restructurings or retraining of workers. However, the GOCV should study the alternatives to identify the most appropriate option.

2. CABNAVE

Cabnave, Estaleiros Navais de Cabo Verde, S.A.R.L., was founded in May 1980 to manage the ship repair yard. Cabnave initially was a partnership between Cabmar, a wholly-owned state enterprise, and Dutch, Portuguese, and local private investors. Currently, Cabmar owns 87.5 percent of the company, and the remainder is owned by Dutch and local private interests. Cabnave is based in Mindelo.

Ship repair is not a strategic industry in Cape Verde. Therefore, several privatization options should be considered. One option would be to merge Cabnave and Cabmar, thereby combining the shipyard installations and the repair operations. Another option to consider would be a management contract.

3. FAMA

Fama, Fábrica de Massas de Cabo Verde, S.A.R.L., was founded in December 1982 to produce pasta and other wheat flour products. The Government of Cape Verde owns 20 percent of the company and private investors own the remainder. Fama is based in Mindelo.

Although Fama is a food producer, pasta is not a staple food, so the company is not considered strategic to the Government of Cape Verde. Because Fama is not currently profitable, it may be difficult for the GOCV to sell its interest in the company. One privatization option, therefore, would be to restructure Fama to prepare it for eventual sale. Such a restructuring would include the renegotiation of bank debt. Liberalization of pricing policy by the GOCV also would help create conditions favorable for privatization of Fama. Alternatively, the GOCV could attempt to sell its interest in Fama and let the new owners address the firm's problems.

The privatization options should be carefully studied in order for the GOCV to achieve the maximum benefit from the privatization.

4. HOTELMAR

Hotelmar was established in July 1978 to build and operate hotels in Cape Verde. The firm is 51 percent owned by the GOCV and 49 percent owned by private investors. Hotelmar is based in Praia.

Because the tourist industry is targeted for development, the GOCV should consider privatization of Hotelmar. One attractive option for the short-term would be a management contract or lease. There is a precedent for such an arrangement in the Novotel lease of the Hotel Belo Horizonte in Sal. An outside firm could improve the firm's operations and restore Hotelmar's profitability. A restructuring of the firm also should be considered. At a later date, other privatization options could be implemented, such as a share sale, management buyout, employee stock ownership plan, or some combination of these alternatives. Further study is needed to determine the feasibility of the options and to select the appropriate path for privatization.

5. MORABEZA

Morabeza, S.A.R.L., was founded in March 1978 to manufacture garments. Until recently, the Government of Cape Verde owned 28.8% of the company, with private investors holding the remainder. Late in 1991, Morabeza initiated a debt for equity swap which will give the GOCV a controlling interest of 50-55% in the firm. Morabeza is located in Mindelo.

Morabeza has begun to take steps to improve its fragile financial condition. The company needs to improve its operating efficiency to compete effectively in international markets. Because the clothing industry is not strategic, the GOCV should consider divestiture of Morabeza. There are several possible privatization options that should be studied including a joint venture between Cape Verdean and foreign investors, outright sale, management buyouts, and employee stock ownership plans. The feasibility of each option needs to be analyzed and a company valuation needs to be prepared in order for the GOCV to select the best option for privatization.

6. SITA

Sita, which is based in Praia, was founded in October 1983. The firm began producing paints in 1985. The Government of Cape Verde owns 20 percent of Sita. Private investors, including the general manager, own the remaining 80 percent of the firm. It is interesting to note that Shell of Cape Verde owns 10 percent of Sita and conducts regular audits of the firm.

The GOCV has enjoyed a profit on its investment in SITA. Based on the Government's development plan, there is no strategic reason to retain this investment. The GOCV should consider selling its ownership interest in SITA. Existing investors, employees, and management may be interested in purchasing the GOCV's portion of Sita. Profits gleaned from this sale could be used to help restructure other SOEs or to implement other phases of the privatization plan, such as retraining of workers.

SECTION III

RECOMMENDATIONS FOR PLAN OF ACTION

This recommendation section proposes the steps the GOCV needs to follow, discusses the financing aspects of privatization and suggests the plans of action for USAID and other donors' interventions. The recommendations are based on the lessons learned from other countries and are specifically tailored to Cape Verde's requirements.

I. PRIVATIZATION STEPS

In order to enhance the likelihood of success in its privatization efforts, the GOCV needs to follow the following steps:

1. Formation of a privatization organization
2. Definition of the national objectives and priorities
3. Development of a privatization policy, strategy and guidelines
4. Evaluation of SOEs performance and selection
5. Valuation of SOEs
6. Selection of the methods of privatization for each SOE
7. Identification and selection of bidders
8. Negotiation and execution of transaction
9. Monitoring of post-privatization performance
10. Adjustments

Each step needs to be studied carefully because the impacts must be anticipated for the privatization program to be successful.

A. Formation of Privatization Organization

Because the privatization process is very tedious and requires substantial resources and time, a full-time organization needs to be formed, which can devote its full attention to the privatization process. Part time or ad-hoc committees like the ones in Rwanda, Egypt, Thailand or Sri Lanka have not been successful; in contrast, countries like Morocco, Tunisia or Malaysia realized early in the process that a full-time organization will accelerate the privatization process.

The members of the privatization organization need top political support and technical competence with wide representation from all parties impacted by privatization such as the leaders of the ministries, the business associations, the labor unions and the media. The organization would directly report to the Prime Minister just like a council of ministers with the Minister of Finance and Planning at the head as is the case in most countries. The leaders make decisions on policy formulation and strategy design based on the studies provided by the technical staff.

B. Definition of National Objectives and Priorities

Before entering into a privatization program, a thorough understanding of the program's objectives and expected benefits is essential. It is vital that the GOCV leaders are prepared for the wide-ranging impact that privatization will have on the national economy so they know how to brace for the change. From the policy perspective, understanding the goals of privatization is essential so that the policy-makers who are overseeing the privatization transactions can judge the effectiveness of privatization and derive lessons from the experience. Because this step is the most important one, a more thorough discussion is provided in this preliminary assessment.

In the implementation of the privatization program, the following objectives can be obtained:

1) Increase enterprise efficiency and private sector growth

With privatization, efficiency will be improved because managers and workers are held accountable to the shareholders who will monitor their performance better than the governments. One example would be the simple risk of bankruptcy and layoffs in case of insolvency. Also, because there are no longer any government subsidies, capital will have to be raised at a cost and any investment will be subjected to a rigorous capital budgeting process.

Greater efficiency and higher profit stimulates private sector growth because of expansion of existing firms by internal reinvestment with retained earnings as well as because of new entries into the business which promotes competition. With the expansion of the private sector, job demand will increase. Based on the assessment of the financial performance of the SOEs, it appears that Cape Verde needs to give efficiency the highest priority for sustained economic and social development.

2) Relieve the fiscal pressure on the government

With privatization, subsidies to the SOEs are reduced and eventually eliminated. With more efficient privatized SOEs, profitability will give the GOCV taxable income which it did not have before. Both of these situations constitute a big relief on the tight government budget which needs to finance other more crucial areas discussed as follows.

3) Help meet socio-economic policy targets

With increase in tax revenue and less subsidies, the government can finance other social projects such as education or health care. As discussed earlier in the first section of this assessment, more resources are needed in Cape Verde to develop the education base of the country and the basic skills required in order to be able to absorb economic expansion via privatization.

4) Stimulate domestic savings and capital market development

With the expansion of the private sector, demand for working capital and longer term financing will increase. The existing supply of capital will have more choices in terms of investment options. The money market as well as the capital market would have added stimulus for development with such increase in supply and demand for funds. One lesson learned from other countries is the case of Jamaica which successfully undertook privatization through public share offering and stimulated its underdeveloped capital market.

5) Broaden domestic equity ownership

With privatization, shares of stock are made available to the domestic investors. Broadened ownership can strengthen political stability in a democratic society. Broader equity ownership can also be a factor in generating public support for privatization.

6) Attract foreign capital

Privatization through the sale of equity offers the opportunity to bring in needed foreign capital either in the form of portfolio investment or as foreign direct investment. With international business joint ventures, beside fresh capital, technology, managerial skills and new international markets are also provided.

Because some of the above objectives might conflict with each other, the GOCV needs to define its priorities. One example of potential conflict would be between more efficient telecommunication services vs. foreign control of CTT by a majority equity ownership because of national security reason. Another example of conflicting objectives is reduction of subsidies by privatization of EMPA vs. food security.

Togo, Jordan and Egypt are examples of confusion in the setting of national priorities and for that reason, privatization could not take off to create the much needed stimulus from the private initiatives. The lesson learned is that long term national priorities should prevail over short term goals and should determine the privatization policy discussed as follows.

C. Privatization Policy, Strategy and Guidelines Development

Privatization policy determines the direction the GOCV wants to take and strategy provides the means to achieve the goals set out by the policy. Basically, the policy must indicate clearly where the country wants to go and the strategy lays out the plans for how to get there while the guidelines explicitly define the rules of the process. Guidelines help to avoid confusion by tracing out the information flow and the procedures. Basically, the guidelines provide the orderly steps to be taken.

As recommended earlier, efficiency should be the priority factor of the privatization policy and different strategies can be used to overcome the problem of unemployment or food security. One strategy would be to privatize the mixed SOEs first, starting with the ones which have the lowest state ownership in order to avoid an unemployment crisis and then progressively move into those with higher state participation. This is also an advisable approach in order to gradually learn from previous experience. It is also less costly at the outset and it fits well with the lack of financing available during the initial phase.

Based on the above discussions, the issue of "strategic" SOEs is no longer a key policy issue because it can be overcome with the appropriate strategy chosen for privatization. If "strategic" has an economic meaning of "basic" or "necessary" then it can be argued that efficiency becomes even most crucial to the country and privatization of such "strategic" SOEs is a must. If "strategic" has a social and political meaning such as the case of basic food security or unemployment, then the choice of the privatization strategy would help to overcome such issues. In summary, some SOEs could be considered "strategic" in the short run; however, in the long run none of them are and all can be privatized.

Finally, it is recommended that the privatization policy needs to be integrated with other economic development policies for a well coordinated and coherent economic development plan. The privatization strategy needs also to be internally consistent between the components. In general, a privatization policy and strategy tends to be better coordinated if a comprehensive impact analysis is conducted beforehand.

D. Evaluation of SOE Performance and Selection

The evaluation of SOE performance can normally follow the same format used in this preliminary assessment covering the vital signs of the SOEs such as liquidity, efficiency and profitability. This evaluation allows the GOCV to make the selection of target SOEs for privatization based on the objectives it has defined. If the socio-economic objective is long term employment rather than short term one, then temporary labor displacement would not be a constraint in the selection process. If subsidy reduction is the primary objective, then the unprofitable SOEs become the targets. In contrast, the profitable SOEs become the targets if foreign investment is the predominant objective.

E. Valuation of SOEs

Valuation based on the existing assets or the projected income of the SOEs provides the foundation for fair market pricing between the GOCV and the potential investors. Basically, this is a crucial step in the implementation process because both parties must feel that they have received a fair deal post privatization. Because a fair market value is difficult to determine, this step is also the most complicated step in the whole privatization process.

One important lesson learned from other countries such as the ones in Eastern Europe is that the time and resources spent in the valuation of SOEs are an investment rather than an expense because valuation will enable the GOCV to determine a range of values for each SOE in order to be able to negotiate and compromise. Also, since investors can be foreign investors as well as Cape Verdean emigrants, workers and the management of the SOEs or domestic investors, the GOCV can use different prices for different groups in order to provide different incentives.

F. Selection of Privatization Techniques

1. Management Contract and Leasing

Two privatization techniques which allow the transfer of enterprise management without ownership transfer are *management contract or leasing*. These privatization options allow the government to reap the benefits of improved efficiency associated with private management when ownership transfer is not desired or when sale is not possible under existing conditions. In a management contract, the GOCV would have to pay the contractor a fee for the service with or without performance guarantee. In leasing, the lessor pays the GOCV a royalty and takes all the proceeds of the operations. Management contracts and leasing are very popular forms of privatization of hotels in Morocco, Egypt and Jamaica and the results have been very positive. The GOCV might consider studying these techniques for privatization of the hotels, the airline, the shipping and fishing SOEs.

2. Build-Operate-Transfer (BOT)

If foreign capital is needed for expansion or for new projects, privatization could also be done via the *build-operate and transfer (BOT)* technique. This privatization technique allows the dilution of the role of the state and is used in infrastructure projects such as roads, telecommunications, and electricity. In Cape Verde, CTT and Electra are considering several expansion plans and BOT might be one alternative approach to privatization. Basically, a group of sponsors which are interested in operating in Cape Verde might want to have equity participation in the Electra expansion project, or may raise debt financing from the international markets. Private equity financing can also be raised with the domestic investors. The common procedure involves a government guarantee for the full purchase of the power generated at an agreed tariff. At the end of the concession period, the power plants are transferred back to the GOCV at no cost.

3. Equity Dilution

Privatization in Cape Verde can also be done without ownership transfer by issuing new common stock shares to private investors. This would dilute the state ownership over time. This technique is more appropriate with SOEs which are profitable and can attract equity investors.

In Cape Verde, the understanding of stock ownership is still very limited; therefore, this technique might be more appropriate when the offering is targeted at foreign investors.

4. Liquidation

This technique consists of sales of assets instead of shares of stock to the private buyers. Going concern is not the objective of the government and therefore, the products provided by this type of SOEs are not usually socially sensitive. The liquidation of mines in the Philippines provides a good example as the government had already stopped exploring them.

5. Fragmentation

Sometimes, it is necessary to sell part of the assets to private hands in order to streamline the SOEs. One SOE for which this option may be appropriate is EMPA which has a full time security service and a fleet of trucks. Fragmentation would allow government divestiture and provide an opportunity for this service to be provided in a more efficient manner by the private sector. The GOCV may also consider fragmentation to streamline product lines which do not involve donations from other countries or which are not socially sensitive (e.g., construction materials).

6. Common Stock Offering

Shares of the SOE common stocks can also be sold to investors or to the workers directly or through the stock market. Because there is no stock market in Cape Verde, direct sale is the appropriate technique. Employee stock ownership plans (ESOPs) are popular in many countries and the concept already exists in Cape Verde with the case of EMPROFAC. ESOP is a technique used with the hope to provide incentive to the workers for higher productivity. Shares can be given for free to the workers or sold at a discount and/or with financing assistance. Management can also buy out the SOE with the workers' participation.

G. Identification and Selection of Bidders

Once the technique of privatization has been decided, the offer is open to the bidders. At this stage, the GOCV needs to define the qualifications for bidders and the format of the bidding process. In order to enhance the likelihood of success, bidders need to have the appropriate financing capability, the managerial know-how and the required technical expertise to run the business successfully. The selection of the bidders should therefore not be based on the price alone but it should be based on a weighted composite of the above criteria.

H. Negotiation and Execution

At this stage, it is important for the GOCV and the buyers to know the negotiation process of each other because differences in legal understanding and interpretation could lead to delays and even roadblocks like in the case of Argentina with its airline. Negotiation on the price should be based on a range of values for more flexibility, and it is always advisable to attach to the different values some requirements which suit both parties' needs. In other words, the negotiation process should be based on give and take.

The execution of the transaction tends to be more simple in the case of floatation of shares, liquidation, management contract or leasing. It is more tedious with BOT because of the time required to build and control by the GOCV needs to be rigorous to make sure that the plants are on schedule and are within the specifications of the contract. Guarantees, insurance, liquidated damages and compensations should be provided and enforced during the execution stage to cover delays, non-completion and termination.

I. Monitoring Privatization

Privatization is a continuous process which lasts even after the execution of the transaction because "successful" privatization is not equal to how many SOEs have been privatized but rather how many privatized SOEs have met the projected impacts intended by the GOCV. If efficiency is the most important objective, then the performance ratios discussed in Section II should be used to monitor the progress. If training requirement constitutes an integral part of the management contract, then the GOCV needs to find out how many workers have been trained and whether the types and levels of training have met the specifications agreed upon during the negotiation stage.

J. Adjustments

The adjustments made could be internal to the privatized SOEs as well as external such as the necessity to relax or eliminate price control, the enforcement of accounting standards, the adjustment of the labor law, the foreign direct investment laws or the tax laws to encourage investments in new financial instruments such as mutual funds or convertible bonds or preferred stocks.

II. FINANCING ALTERNATIVES FOR PRIVATIZATION

A. Traditional Sources of Financing

Traditionally, Cape Verde has depended heavily on official development assistance from abroad with grants and concessional loans accounting for close to half of GNP, the highest level in Africa. External assistance covers 80% of all the financing of public investment programs of which about 60% is in the form of grants.

1. International Assistance

Foreign assistance consists of around twenty bilateral programs. In 1987, Italy was the largest donor with a total assistance of US$10.5 million followed by Sweden with US$7.3 million then Germany with US$7.2 million, Holland with US$6.5 million and the USA with US$6.5 million.

These countries accounted for about 75% of total bilateral aid. The rest was contributed by other countries such as Switzerland, Portugal, the USSR, Japan, China and France.

Multilateral assistance from the UN amounted to US$20 million in 1987 and constituted the most important source of assistance to the country followed by the EEC with US$7.5 million. In addition, five multilateral lending agencies operate in Cape Verde with the ADB as the most important creditor followed BADEA, the World Bank, the OPEC Fund and the European Investment Bank.

Because of the importance of foreign aid and its downward trend since 1986, more coordination among development programs and international sources of assistance need to be considered. As privatization covers a wide spectrum of sectors, financing could be coordinated by incorporating a discrete budget for privatization itself. For example, privatization financing can be incorporated into foreign investment and export promotion programs since some SOEs have export potential and the privatization of most SOEs will require foreign investment participation. International assistance can also cover other important areas which touch privatization such as assistance funding for the revision of the investment and commercial codes, financial institution and financial market development, SOE restructuring, feasibility studies for new private investment opportunities, training in privatization specifically and in management development in general, and initial venture capital participation in BOT financing of infrastructure development projects.

2. *Transfers by Cape Verdean Emigrants*

In total, the Cape Verdean emigrant population is estimated to be twice as large as the population of the country. Approximately half of these emigrants reside in the United States, while an estimated 300,000 are reported in Europe and Africa. Although total transfers by the emigrants to Cape Verde are believed to be much more sizable than the official deposits made in the national bank, BCV, no accurate official data is available to assess this important source of financing. Unofficial figures estimate that total transfers account for some 10% of the country's GDP. In 1986, total transfers from emigrants was estimated to be approximately ECV1.9 billion. In 1989, such source of funding was estimated to be close to ECV2.8 billion.

Most transfers have been used for personal consumption or home improvement and construction and the rest is deposited in BCV time deposit accounts. In 1985, emigrant deposits amounted to 1.5% of total deposits of ECV3.3 billion. In response to the incentives introduced by the BCV in 1985 for the emigrant deposits with higher interest rates and foreign exchange deposit options, the share of emigrant deposits increased to 8.4% of total deposits of ECV4.4 billion in 1987. One example of an incentive option is in the interest rates paid for foreign exchange deposits, which are allowed to vary according to the prevailing rate in the countries of the respective currencies.

The size and responsiveness to incentives of emigrant transfers described above constitute an important source of financial participation in the privatization efforts of Cape Verde, both in terms of foreign direct investment and more importantly in the form of portfolio investment in other instruments other than time deposits in the BCV, as discussed in the following section.

B. Innovative Sources of Financing

1. Privatization Fund

Experience in other countries has shown that the failure of privatization programs is oftentimes due to the inefficient management of the process. One of the most important deficiencies is the lack of adequate financing. Inadequate financing limits the ability of the government to implement SOE restructuring programs in preparation for privatization, to prepare the redundant labor force for orderly relocation with appropriate training and compensation for dislocation, to obtain expert services for the valuation of SOEs and for the negotiation with buyers to obtain fair market prices.

The creation of a privatization fund would help to budget for financing requirements and to identify the sources of funding needed in order to achieve the objectives set by the GOCV. The creation of a privatization fund would force the privatization committee to plan systematically for various privatization activities and be accountable for their implementation. Finally, any deviations from the budget should be explained and appropriate adjustments made.

The initial funding of the privatization fund could come from the donor community and the GOCV. Proceeds from the privatized SOEs would then replenish the fund and be used to finance further privatization activities. As Cape Verde's only financial institution at this time is the BCV, the privatization fund could be created to include an investment division which would handle the distribution of securities, such as stocks and bonds, resulting from the privatization of SOEs. Such an investment division could very well spin-off into a full scale private investment holding company and a government supervisory agency to oversee the newly privatized firms. Over time, such a government agency could evolve into an institution similar to a securities and exchange commission when the capital market in Cape Verde requires such regulation.

Another option that may be served by the privatization fund is the creation of a mutual fund of securities for several privatized SOEs to provide a diversified risk portfolio option to risk averse investors who do not know very much about investment or who do not have the time to follow their holdings all the time.

2. Innovative Financial Instruments

a. Working Capital Financial Instruments

Short term financing instruments need to be introduced to supplement bank loans to enhance the likelihood of successful post privatization periods. Commercial paper is one possibility which has been used successfully in several countries. One example is the Muqarda Bond in Pakistan.

Factoring of account receivables is another possibility to be studied under the development of a commercial bank to be spun-off from the current BCV.

b. Capital Market Instruments

Beside common stocks, convertible securities such as convertible preferred stocks and convertible bonds can be attractive investment instruments for investors. The convertibility feature can be a good transition tool to develop the culture of investing in securities other than bank deposits, but which has similar fixed income payment feature like that of time deposits. The added incentive is that investors have the option to convert these securities into common stocks once the privatized SOEs prove to be profitable post privatization. The convertible securities can also be good instruments in the earlier stages of privatization to gain investor confidence.

As mentioned earlier, SOE shares can be grouped together and distributed as mutual fund shares. This option allows for the diversification of risk as well as professional management. This option can be very attractive to the emigrant community who are already familiar with this investment instrument. Mutual fund shares can also attract institutional investors, as proven by the successful experiences of the Mexico Fund and the Thai Fund among the emerging market funds.

3. Employee Stock Ownership Plans (ESOPs)

Employees can participate in the privatization process of their SOEs by owning equity shares of their respective firms. Ownership can be a good indication of commitment to the betterment of the SOE post privatization, and an incentive for higher productivity as profitability is shared among the owners at the end of the year. ESOPs will be made accessible to both management and workers, and issues such as the pricing of shares and percentage allocations require further study.

To finance share acquisition, the privatization fund and/or a private bank can provide loans to workers and others without adequate funds in the initial stages of the program. Loan repayments can be made over time with deductions from monthly salaries, as is the practice under the social security system. At the end of the year, a predetermined portion of the dividend could also be used to amortize the loan.

4. Build-Operate-Transfer (BOT)

To develop new infrastructure or expand existing facilities, BOT can be an innovative source of financing privatization. Such projects have been implemented in Pakistan, Hong Kong, and Turkey for the energy sector, and for the telecommunications sector in Mexico. Groups of venture capital investors participate in the initial funding of the project, in the construction of the project, and in running the project for a number of years. At the end of the contracted period, the plants are transferred to the government. This method of financing provides speed and availability of funding which normally is not accessible to a country, particularly when it is necessary to deal with the international capital market.

III. ACTION PLAN FOR USAID AND OTHER DONORS

Because the availability of funding privatization efforts in Cape Verde can be limited compared to other countries, the following activities recommended in the action plan can be undertaken as separate and discrete tasks.

A. Long Term Advisor

A long term advisor is needed to assist the GOCV from the beginning to the end of the privatization process because of his/her experience and expertise which are needed in Cape Verde. Experience in other countries has shown that a full-time advisor provides continuity as well as depth because of his/her knowledge about the country over time. This necessity has been recognized in Indonesia, Tunisia, Morocco and many other countries which have met success in their privatization efforts.

The long term advisor needs to have both a macro as well as a micro-economic and financial background in order to be able to deal with all aspects of privatization. The person needs to be able to deal with both policymakers and the technical staff and should be able to coordinate the two in the formulation of privatization policy, in the design of strategy and in the implementation of the guidelines.

B. Case Study of SOCAL

Because the shoe company SOCAL was privatized in 1989 and more importantly since it has the elements of exports, foreign participation, labor problems, and experience with a full business cycle with fluctuating sales, it is the ideal candidate for lessons learned from a case study.

The case study needs to be conducted immediately during this initial phase because of the practical application of the lessons learned to policy formulation, strategy design and guideline development. It can also be used as a practical tool for training discussed as follows.

C. Training in Privatization

During the initial phase of the program, basic training in privatization is required so that the policymakers as well as the technical staff are exposed to the fundamentals of privatization such as the various techniques of privatization, the estimation of privatization cost and financing requirements, the various sources of financing, the ESOP options, the basics of negotiation and public relations. This type of basic training can last between five to ten days depending on the budget available. More depth will be covered with a longer training period and case studies can be used for practical hands-on exposure.

At the second phase, more advanced technical training will be needed such as training on the techniques of valuation or on BOT. This type of training is tailored to the technical staff and the duration can vary between two to five days depending on the budget made available.

D. Applied Research

At the initial phase, applied research on labor redundancy is required in order to assess the possible impacts on labor based on different scenarios of privatization. This type of study will allow the GOCV to chose the strategy which seems to best fit the country in consideration of the predicted impacts. With the results of applied research, monitoring of the impacts and adjustments is facilitated.

During the initial phase, studies need to be done in the area of financial sector development because of the situation in Cape Verde. Beside a study on how to develop other financial institutions, new financial market instruments need to be explored.

Another area of applied research which can be done either at phase one or two is the possibility of setting up ESOPs in privatization. This study will determine which type of SOEs would be most adaptable and will provide some guidelines in terms of pricing of shares, percentage of ownership, financing the ESOP funds, amortization of the loans and leveraged management buyouts.

E. Valuation of SOEs

Because a fair market value is crucial to both the sellers and the buyers, an enterprise value needs to be determined in a rigorous fashion. Reliance on book value, which is simply an accounting concept based on historical cost, can be quite misleading. More sophisticated methods such as discounted cash flow method might be used because it relies on future cash flows projected with a more realistic assumption of efficient private management.

F. Information Dissemination

Transparency of the privatization process is a prerequisite for success. Information dissemination via public relations is mandatory to educate the public about the long term benefits of privatization and to sensitize the workers to the possible short term sacrifices.

The establishment of a documentation center is another important aspect of the privatization initiative. The documentation center will serve as a central depository for resource materials on privatization, ensuring that information is readily available to practitioners and others involved with the program. In addition to supporting the efforts of the privatization committee, the center can contribute to general information dissemination activities by making resource materials available to the public.

APPENDIX

PERFORMANCE OF STATE-OWNED ENTERPRISES

Wholly-Owned Enterprises

1. ARCA VERDE

Arca Verde's freight revenue is equally divided between international and domestic business and accounts for roughly 42 percent of total revenues in 1990. Nearly 80 percent of the freight business is with EMPA, another SOE, which distributes food in Cape Verde. The remaining revenues consist of passenger and rental revenues in roughly equal proportions.

Private competition exists in the domestic cargo business, but not in inter-island passenger transport. Portuguese shipping companies represent Arca Verde's most significant international competition, because their ships stop in Cape Verde en route to other countries, giving them a cost advantage.

Arca Verde has 137 employees, 96 of whom are sea-going staff, such as captains, sailors and deck hands. The remaining staff includes one managing director, one representative in Mindelo and 39 additional workers spread among the main office and the Arca Verde offices on each island. Staff levels are higher than needed according to management. Operating efficiencies could be improved in sea- and land-based personnel.

As shown in the Summary Performance Table, Arca Verde has poor profitability in all areas with the exception of its gross profit margin which averaged 83.1 percent. The average operating profit margin was -38.5 percent while the net profit margin averaged - 46.6 percent. These measures indicate reasonable sales and production costs, but poor operating costs and financial management. As a result, the accounting return on asset ratio (AROA) was -15.5 percent and the accounting return on equity averaged -33.1 percent. All standard deviations are small indicating that the mean values are acceptable.

As a shipping company, Arca Verde is capital-intensive, so cashflow analysis is required to interpret the company's results. Adding back depreciation to net income reveals a cash ROA of -1.3 percent and a cash ROE of -3.3 percent. The cashflow approach presents the company's situation more realistically than does the accounting approach, particularly when depreciation constitutes an important portion of expenses.

These profitability measures are not surprising because all the liquidity and efficiency measurements indicate that Arca Verde is rather inefficient in all areas of management. In marketing management, accounts receivables are 191 days outstanding causing liquidity to average 0.42. As a result, Arca Verde lagged its payments to creditors by more than eight months, as its notes payable outstanding are 245 days. Fixed asset turnover was only 0.46 and

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total asset turnover was only 0.33. Because inventory for a shipping company primarily consists of spare parts and some small items not requiring significant amounts of working capital, the inventory turnover ratio of 49.3 is high.

Arca Verde's debt ratio was reasonable, accounting for just over 50 percent of assets. However, because the company has losses, the times-interest earned is negative at -6.17 percent.

2. CTT

CTT domestic service is of medium quality. The major complaint about the company is the delay for installation of new service which can range from one week to one year. CTT is reaching capacity constraints: there are a limited number of new lines available and local switching capacity is working near its limit, especially in Praia. International service is of mixed quality. While telephone calls to the United States are made with little difficulty, calls to Europe and continental Africa often require several attempts. CTT is nearing its international capacity constraint. The company uses a submarine cable to Portugal, handling five lines, and an INTELSAT B Standard B satellite earth station with capacity currently being expanded to 58 circuits. Data communications, such as fax, also often require several transmissions to complete and are very expensive. CTT is aware of the need to invest in infrastructure to expand capacity and is currently considering several proposals for new equipment from international telecommunications suppliers such as AT&T, Marconi, and Alcatel.

In addition to investing in equipment, CTT plans to invest in employee training. Sophisticated technical training for the telecommunications industry is not readily available in Cape Verde, so CTT operates its own educational programs. The company has 666 employees, including directors, administrative staff, technicians, and workers. These numbers appear high for the size of the company. For example, CTT has mechanics and carpenters on staff. The company is also staffed to allow for employees' sick leave and vacations. As a result, CTT could reduce its staff by contracting out for services such as carpentry and vehicle repairs.

CTT is a very profitable company, as is evident from the summary table. The company's gross margin averages 99.0 percent because telecommunications is a service industry, so the firm does not manufacture goods for sale. Although demand and sales are robust, the company is not particularly efficient, as the operating margin averages 17.5 percent. Further evidence of weak financial management can be seen in CTT's accounting ROA of 2.8 percent and accounting ROE of 7.8 percent. The standard deviations are low, so these figures are reliable.

Telecommunications is a capital-intensive business, with heavy investment required in networks and equipment. Consequently, it is important to examine the firm's cashflow to gain a deeper understanding of its operations. Adding depreciation to net income shows that CTT's cash return on assets is 17.8 percent and its cash return on equity is 35.1 percent. These ratios indicate a healthy cash flow, but also indicate a need for further investment in infrastructure.

While CTT is profitable and enjoys a strong cash flow, the firm's marketing and financial management ratios point out inefficiencies. At first glance, liquidity appears reasonable at 1.54 times, however, this is misleading since accounts receivable collections are slow. Days sales outstanding average 224 days, meaning that the firm takes slightly more than seven months to collect from customers. Fixed asset turnover of .55 times and total asset turnover of .38 times are low for the telecommunications industry, indicating operating weaknesses. Inventory turnover may appear high at 96.1 times, however, because telecommunications firms are services companies and have low inventories, this ratio is not unusual.

Debt comprises 63.0 percent of total assets and CTT's interest earned is 2.65 times which is reasonable.

3. ELECTRA

Electra produces electricity primarily using diesel generators. Capacity in the major cities of Praia, Mindelo, and Sal should be adequate to meet demand over the medium term. Electra is installing two new 3.3-megawatt (MW) generators in Praia, which will add to the current capacity of 4.4 MW. Mindelo also has two 4.4 MW generators plus two secondary generators each with 1.1 MW capacity. An additional 300 KW of power can be generated by wind power. In 1993, Electra plans to add two new 3 MW generators in Mindelo. Sal has a combined capacity of 2.5 MW at present and is adding another 1 MW generator.

The company's electrical service offers reasonable quality. Blackouts are infrequent, although voltage may fluctuate up to 15 percent. Costs of electricity are quite high, with industrial users often paying more than double the prevailing rate in industrialized countries.

Electra's water service provides desalinated water in Mindelo and Sal. Demand in Mindelo currently exceeds supply. Electra increased its production capacity in Mindelo to address the need for additional water. Supply in Sal currently meets demand. Desalinated water is costly to produce, causing high water rates in Sal and Mindelo.

Detailed information on staffing levels was not made available to the team.

Electra's performance, as shown on the summary table, is inefficient. Electra's average gross margin is 54.7 percent, but its operating margin averages only 7.2 percent and its net profit margin is 6.0 percent. These ratios indicate that Electra's raw materials costs and financial management practices are reasonable, but that it has high operating expenses. The accounting ROA and ROE of 1.6 percent and 2.1 percent, respectively, confirm that Electra need to improve its efficiency.

It is instructive to look at the company's cash flow because depreciation is a significant portion of operating expenses. When depreciation is added back to net income, a cash ROA of 6.9 percent and a cash ROE of 9.1 percent are revealed. These figures are well above the market averages for the Cape Verde industry as a whole.

The current ratio of 1.98 times indicates high liquidity, although most of the company's liquidity is tied up in accounts receivable. Marketing management could be improved as days sales outstanding averages 194 days, or more than six months. Net purchases outstanding are roughly the same, averaging 199 days.

Times interest earned averages 6.94 times, but this measure has dropped sharply in recent years, indicating an increase in leverage. However, Electra's debt comprises only 24.5 percent of total assets, which is low for a utility.

4. EMPA

EMPA imports food products and construction goods in Cape Verde. The company's primary food imports are corn, rice, sugar, cooking oil, and milk. Imports of construction materials include cement, wood, iron, and steel. EMPA has the exclusive right to import corn, sugar, cooking oil, and cement to Cape Verde. For other products, EMPA's imports constitute about 95 percent of the market. EMPA also plays an important role in the storage and distribution of food aid from multilateral organizations and donor countries.

In addition to importing essential goods and storing food aid, EMPA assures their distribution to all the islands of Cape Verde. EMPA operates as a wholesaler, selling goods to retailers. Until recently, EMPA also had stores where its products were sold in large and small quantities. With the closure of these stores, EMPA now supplies retailers with the same goods in small packages for sale to the individual consumer. Prices are regulated to assure that prices are equitable to all Cape Verdeans, regardless of their place of residence.

EMPA has offices in Praia and Mindelo. The firm has significant investments in storage facilities, such as grain silos in Praia and Mindelo, a fleet of trucks in Praia, São Tiago and on other islands for distribution, warehouses, and a workshop. The firm uses Arca Verde to ship goods among islands.

EMPA has 1,025 employees. The firm has been letting workers go gradually. 21 workers were released in 1991; an additional 30 workers will lose their jobs in early 1992. EMPA has workers in the following functions: security, inspection services, information systems, imports, finance, human resources, operations, and technical support. EMPA could operate effectively with far fewer employees by using outside contractors to provide services.

From the Summary Performance Table, it is apparent that although EMPA is profitable, the firm is not particularly efficient. Gross margin averages 23.7 percent, indicating reasonable acquisition costs of goods. The firm's average operating margin of 7.0 percent and net profit margin of 3.7 percent point to inefficiencies. Personnel expenses and third party expenses, such as fuel, electricity and distribution expenses are significant for EMPA. Accounting ROA averages 4.7 percent and accounting ROE averages 15.6 percent, both respectable levels. It is important to note that these ratios have relatively high standard deviations, which limits their usefulness.

Because EMPA incurs depreciation expenses, it is instructive to look at its cash flow. Adding depreciation back to net income reveals the firm's strong cash flow. EMPA's cash ROA averages 6.7 percent while its cash ROE averages 22.6 percent.

Liquidity, shown by the current ratio, is adequate at 1.32 times. However, a large portion of the company's current assets is tied up in inventories. This is evident from EMPA's inventory turnover ratio of 2.56 times. Fixed asset turnover is 5.25 times, while total asset turnover is 1.28 times. EMPA's marketing management is good, with clients paying bills in 28 days, on average. EMPA, on the other hand, pays its suppliers in 131 days.

Debt comprises 71 percent of total assets, which is notable. The firm's coverage of interest paid is more than adequate averaging 19.0 times, although coverage slipped to 6.0 times in 1990.

5. EMPROFAC

Emprofac produces antibiotics, analgesics, decongestants, antihistamines, and other medicines in various forms, such as tablets, capsules, and ointments. The company imports most of its raw materials for production from European suppliers, primarily Portuguese, Spanish, German, and Dutch, although some supplies are obtained from Brazil. Information regarding capacity utilization is not available at present. Emprofac maintains high standards of quality control.

In addition to being a manufacturer, Emprofac is also a wholesaler and retailer. As a wholesaler, the company sells to pharmacies, hospitals, and the medical community in Cape Verde. Emprofac also has exported some products to Lusophone Africa, primarily to Angola. Exports are a minor component of sales and export growth prospects are limited due to competition. As a retailer, Emprofac owns and operates pharmacies in Mindelo and Praia and has outlets or "postos de venda" in other towns. Pharmaceutical prices are regulated by the GOCV.

In 1991 a new company, Laboratórios Inpharma, S.A.R.L., was formed to produce pharmaceutical products. Inpharma is a joint venture 40 percent owned by Emprofac, 40 percent by the Portuguese company LABESFAL, and 20 percent by private Cape Verdean investors, including Inpharma management. Inpharma is to take over production of pharmaceuticals, leaving Emprofac to market and sell them. As of December 1991, this change had not occurred as Inpharma's installations were still under construction.

Staffing information is not available for either company. Emprofac will transfer about 24 production workers when it transfers the equipment to Inpharma.

Emprofac is a profitable company which has enjoyed healthy earnings. The company's gross margin averages 39.9 percent, while its operating margin averages 12.5 percent and its net profit margin is 6.8 percent. These margins indicate that raw materials costs are relatively high, probably because of the high import content. Operating costs are a little on the high side, but financial expenses are still under control. Emprofac's returns indicate that its performance is reasonable: the mean accounting ROA is 7.5 percent and the mean accounting ROE is 13.1 percent. The ROE is only slightly lower than some pharmaceutical companies in developed countries. However, it is important to note that pharmaceutical firms in developed countries invest heavily in research to create new drugs, whereas Emprofac does not.

The pharmaceutical industry is moderately capital-intensive, therefore it is useful to examine Emprofac's cash flow. When depreciation is added back to net income, a cash ROA of 10.4 percent and a cash ROE of 18.1 percent are revealed. These figures indicate a strong cash flow.

The liquidity measure reflects cash flow. Emprofac's current ratio is 2.41 times, indicating high liquidity. Emprofac's efficiency measures show that the firm's performance is mixed. Inventory turnover averages 2.85 times, indicating fairly high inventory levels. These high inventory levels may be necessary to assure continuous supplies of critical medical goods in Cape Verde. The firm's asset turnover ratio averages 1.10 times, which indicates low utilization of assets. Since Emprofac primarily serves the Cape Verdean market, this figure is not surprising. Emprofac's cash management is also inefficient. Days sales outstanding average 67 days while net purchases outstanding average less than 7 days, which means that the company pays its bills faster than it collects from its customers.

Interest earned averages over 300 times. However, it is important to note that bank loans have grown over the last year as Emprofac has not repaid the principal of certain loans to the Bank of Cape Verde, which could cause financial expenses to rise significantly in the future. Emprofac's total debt ratio is conservative, averaging 42.4 percent of total assets.

6. ENACOL

Enacol sells jet fuel, gasoline, fuel oil, butane gas, lubricants, and other petroleum products in Cape Verde. Historically, jet fuel has been the company's most important product, generating between 47 and 60 percent of revenues. Sales of jet fuel declined sharply in 1990 for two reasons. First, Cuba, Enacol's most important client, reduced its consumption as Cuba withdrew personnel and support from Angola. Second, the Gulf War caused an overall decline in air travel, lowering jet fuel purchases. Other important purchasers of jet fuel are Aeroflot and TAAG (Transportes Aéreos de Angola). Gasoline is the firm's next most important product, accounting for approximately 23 percent of sales. Fuel oil sales comprise roughly 19 percent of sales. Butane gas, lubricants, and other products make up the remaining sales. Prices of Enacol products are regulated.

Enacol imports its supplies of petroleum from foreign oil companies. Important suppliers are Petrogal, Addax, Chevron, and Sitco. Enacol also purchases services from Shell in Mindelo and Sal. Because Shell has the exclusive right to operate in Sal until the end of 1996, Enacol must use Shell's installations for storage and supply of fuel to airplanes. Services rendered by Shell were the single biggest expense for Enacol from 1985 through 1989. Detailed expense information for 1990 was not available.

Personnel expenses are also a major cost component. It is interesting to note that Enacol has a market share of approximately 30 percent and has 125 employees, whereas Shell has a 70 percent market share and 75 employees.

Financial expenses also are significant for Enacol. The firm has relied heavily on the Bank of Cape Verde for funding over the last two years. Bank loans doubled from 1989 to 1990 as the company used debt, in the absence of cash, to acquire inventory.

Enacol's overall profitability has been poor, as is evident in the summary performance table. Although Enacol has a favorable gross margin of 30.7 percent, indicating its petroleum costs are reasonable, the firm's operating margin drops sharply to .4 percent and its net profit margin drops further to -6.2 percent. These margins reveal that the firm is not managing its operating expenses efficiently and that financial management is poor. As mentioned above, costs of services provided by Shell and personnel expenses are high. Consequently, Enacol's accounting ROA averages -5.3 percent, while its accounting ROE averages -616.1 percent. Standard deviations for the profitability ratios are high, indicating a high variability in performance over the three year period. It is instructive to note, however, that this variability results from a wide but consistent downward trend in the company's performance.

The oil industry is fairly capital intensive, so it can be instructive to examine cash flow. Adding back depreciation to net income shows the firm's cash ROA to be -1.8 percent. Cash ROE, however, averages -379.0 percent. Because Enacol has sustained large losses over the last two years, its equity has nearly been depleted, magnifying the impact of its negative cash flow.

Average liquidity is measured by the current ratio which averages .93 times. Days sales outstanding average 148 days, meaning that it takes clients nearly five months to pay bills to Enacol. The company pays its suppliers a little more quickly than it is paid by clients, indicating a mismatched cash flow, as net purchases outstanding average 126 days. This ratio has deteriorated over the last three years, a symptom of Enacol's financial difficulties. Enacol's asset management ratios also indicate that the company is not run efficiently. For example, although Enacol turned over its inventory 4.36 times per year on average, which compares favorably with Shell's ratio of 4.49 times, inventory turnover has declined over the three year period with a low of 2.56 times in 1990. Fixed asset turnover of 3.04 times and total asset turnover of .91 times are also comparable with Shell's, however, these ratios have also declined significantly over the last year.

Similarly, Enacol's average debt to total assets ratio of 89.3 percent shows that the firm has relied on debt to deal with its cash crunch. The combination of poor performance and increasing reliance on debt financing is reflected in an average interest coverage ratio of .08 times. This figure indicates that the company generates earnings barely in excess of its obligations to its debtholders.

7. ENAVI

Enavi supplies chicks as well as vitamins, medicines and chicken feed to farmers who raise chickens. The firm has no competitors in the incubation and supply business. Enavi imports eggs for incubation from Holland at a low price. Vitamins and medicines for chickens are imported in bulk from Portugal at favorable prices. The vitamin and medicine business, although small, is highly profitable for Enavi.

Enavi is also a poultry and egg producer. In Praia and Mindelo, the firm is the dominant supplier. It is interesting to note that farmers, who generally purchase their chicks and supplies from Enavi, are competitors in the market for poultry products. Other competitors are importers of frozen chicken, such as retailers.

Enavi has 74 full-time employees in Saõ Tiago. Of these totals 29 are engaged in administration, 5 in incubation, 18 in the slaughterhouse, 7 in the feed area, with the remainder tending chickens. These levels are high for Enavi's activity levels. Labor accounts for about 30 percent of the production cost of each egg. It is estimated that Enavi would operate effectively with half the number of staff.

Enavi's performance, as shown on the summary table, shows that the firm is somewhat inefficient. Enavi's gross margin of 41.6 percent indicates a healthy sales volume and reasonable production costs, but the firm's operating margin of 6.3 percent point to high operating costs. Inefficiency in financial management is also evident, although less severe, as reflected in the average net income margin of .4. The average accounting ROA of .2 percent and accounting ROE of .3 percent confirm that there is room for Enavi to improve its operations. Since these figures represent the averages for a year in which the company's net income was negative and one in which net income was positive, the standard deviations are high.

Since depreciation is an important factor in operating costs, examining the company's cash returns is instructive. Cash ROA averages 6.7 percent, while cash ROE averages 11.1 percent, indicating Enavi has a healthy cash flow.

The liquidity measure yields a similar result, demonstrated by its current ratio of 1.78 times. Asset and marketing management leave room for improvement. Inventory turnover of 4.16 times is low, even when allowances are made for the small Cape Verdean market. Fixed asset turnover of 1.59 times and total asset turnover of .89 times indicate underutilization of assets or overcapacity. Days sales outstanding are reasonable, averaging 34 days. Net purchases outstanding are closely aligned with sales, averaging 29 days.

Total debt comprises 39.6 percent of assets, a reasonable level for this industry. Interest coverage of debt is more than adequate at 8.74 times.

8. FAP

FAP produces, imports, and distributes agricultural products, seeds, equipment, and supplies, and exports bananas. Specifically, FAP has animal feed, milk, and water pump factories. The company also imports pesticides, fertilizer, animal medicine and other agricultural equipment and supplies. FAP operates as both a wholesaler and a retailer, selling some of its products at its own shops. The remaining products are sold through cooperatives and small retailers.

With a few exceptions, such as banana sales, FAP's sales tend to be higher when agriculture does poorly. The reason for this trend is because when the harvest is poor, grazing conditions are also, requiring farmers to purchase animal feed. FAP's sales vary from year to year. In 1990, animal feed was the largest component of sales, accounting for 34 percent of revenues. The firm's next most important product was bananas, comprising nearly 27 percent of sales. Bananas are exported primarily to Portugal. In the last year, competition from Central America has caused FAP to suffer losses on its banana exports. This loss occurred because FAP must pay a fixed price for bananas in Cape Verde, but must sell at the market rate, which fluctuates.

FAP has no significant competition in most of its other products, with the exception of animal feed and milk. Justino Lopes is a major competitor in the animal feed market, while there are various competitors in the milk market, as dried and UHT milk are imported for retail sale in Cape Verde.

Prices of many of the products sold by FAP are regulated. Because the company was established to promote agricultural development, it is only legally permitted to earn a 15 percent margin on its wholesale business, such as banana exports. If FAP earns a margin greater than 15 percent on its banana sales, for example, the excess profits are distributed to its banana suppliers.

FAP has 70 workers. Staff is broken down as follows:

Animal feed production	7
Milk production	10
Workshop	14
Commercial department	17
Administration	22
Total	70

At current levels of capacity utilization, it is estimated FAP could operate effectively with about 45 workers.

FAP is not profitable, as is evident from the Summary Performance Table. Although gross margins average 26.0 percent, this level is low for the Cape Verde market in general. The firm's costs of goods sold are reasonable, but operating expenses are high, causing an average operating margin of -5.3 percent and an average net profit margin of -5.7 percent. FAP's

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accounting ROA of -7.3 percent and accounting ROE of -89.1 percent are symptoms of the firm's low capacity utilization and poor operating efficiency. It is important to note that ratio averages are based on performance figures for two periods in which the company's bottom line results were highly variable. The standard deviations for these profitability ratios are therefore significant.

It is instructive to look at cash flow, as well, because FAP is moderately capital intensive. FAP's cash flow is negative, even after depreciation is added back to net income. As a result, the company's cash ROA is -3.2 percent and its cash ROE is -57.0 percent. Standard deviations for these figures are significant.

FAP appears to have high liquidity with a current ratio of 1.88, however, much of this is tied up in inventory, which has a low turnover, and accounts receivable. Due to a significant reduction in government loans in 1990, the company's current liabilities figures are highly variable, and the standard deviation for the current ratio is high. FAP's marketing and asset management measures indicate that the firm does not operate at optimum efficiency. Inventory turnover averages 3.6 times. The broad variety of products sold by FAP complicates inventory management. Fixed asset turnover averages 7.0 times, but total asset turnover is 1.19 times, which means that FAP has high inventory levels. FAP's customers, in general, take over six months to pay their bills, as days sales outstanding are 139 days. The firm pays its bills in about two months, as net purchases outstanding are 61 days.

FAP relies heavily on debt, as is shown by its debt to total asset ratio of 82.9 percent. Because the firm is not earning income, its interest coverage is -3.45 times. Standard deviations for both of these averages are high due to the abovementioned debt reduction.

9. INTERBASE

Interbase derives 85 percent of its revenues from selling fish and lobster. The remaining revenues are generated primarily by sales of ice and refrigeration services. Fish account for 57 percent of the total, while lobster account for 29 percent of revenues. The company sells fish in the international and domestic markets. Prices in the international market are competitive, while those of the domestic market are regulated by the Government of Cape Verde. Interbase historically relied on one customer, Algeria, for as much as 90 percent of its fish sales. Recently, Algeria has reduced its purchases from Interbase, so the company needs to diversify its customer base. Interbase obtains fish from domestic fishing companies to sell. Pescave, another SOE, has been one of Interbase's largest suppliers of fish and seafood.

Interbase has installations in Sal and Mindelo for refrigeration and storage of seafood. Capacity utilization is estimated to be 30 percent. At these installations, the company also makes ice which it sells to fishermen and other clients. Interbase has no facilities to process or can fish or seafood products. The firm has a total of 163 workers in Sal and Mindelo. Personnel expenses are the largest category of expenses after the cost of raw materials. Staffing levels appear high for the level of economic activity.

The Summary Performance Table indicates weak profitability, with the exception of its gross margin of 56.4 percent. Operating expenses are high, especially wages and salaries, causing the operating profit margin to average 5.5 percent. The net profit margin was negative, largely due to the company's depreciation expenses. Further evidence of Interbase's poor financial and operational experience can be seen in its average accounting ROA and ROE of 2.3 percent.

Examination of cash flow is instructive because Interbase is moderately capital-intensive. Adding depreciation back to net income reveals an average cash ROA of 5.9 percent and average cash ROE of 6.6 percent. The standard deviations for these averages are low, indicating that the numbers are meaningful.

Many of the liquidity and efficiency measurements indicate that Interbase's performance is sluggish. It is important to analyze these measures carefully, because some of the standard deviations are significant. For example, Interbase's current ratio of 6.24 indicates extremely high liquidity, however, one account receivable for capital not yet paid in comprises nearly 40 percent of current assets. This same account also causes days sales outstanding to average 356 days, or almost one year. Net purchases outstanding, on the other hand, average 144 days, implying a mismatched cash flow and weak financial management. Inventory turnover of 4 times is low for a distribution company, which by definition must sell and replenish inventory in order to make money. Fixed asset turnover of 1.35 times and total asset turnover of .50 also point to operating deficiencies and poor capacity utilization.

Interbase's debt ratio of 16.7 percent is conservative. Interest is earned on average 5.25 times; however, this measure should be used with caution as the standard deviation is high because the number ranged from positive to negative over the years.

10. PESCAVE

Pescave's principal products are fish and seafood, comprising approximately 80-90% of revenues in any given year; boat rentals and repairs account for the remaining revenues. Tuna are approximately 90% of fish and seafood revenues, while lobster and bottom fish constitute the remainder. According to management, Pescave sells fish below cost through its sister enterprise, Interbase, at fixed prices. Earlier this year, Interbase decided to store fish and seafood prior to sale, acting as a broker, rather than to buy fish outright from producers. This change could aggravate Pescave's financial difficulties as Pescave's cash flow relies heavily on advances from Interbase. Pescave's major domestic competitors are small private fishermen. International competition from developed and developing countries is also acute.

Pescave owns a fleet of eleven fishing boats: four 16-meter boats, four 22-meter boats, and three special 39-meter boats equipped with refrigeration. Only two of the 39-meter boats are currently operational. According to management, its boats are slow and not particularly fuel-efficient. Pescave uses its boats to catch fish off the shore of Ivory Coast during the season from July to November. During the off-season, Pescave sends out only one boat to catch bottom fish in local waters. Based on this information, capacity utilization appears low.

Pescave has 59 permanent employees. Staff breaks down as follows:

Directors	3
Administrative staff	9
Workshop staff	21
Crew (fishing)	26
TOTAL	59

Pescave also hires additional fishermen during the season to meet demand. By using seasonal workers, the enterprise can keep staff levels lower than if they staffed for peak labor demand. Nevertheless, staffing levels appear to be high. Personnel expenses comprise the largest portion of operating expenses, exceeding revenues. This problem has two causes: first, Pescave receives fixed prices for its fish and seafood; second, Pescave's fishing boats are labor-intensive, requiring higher levels of staff than international competitors, with more modern equipment.

Pescave has been running a deficit since inception. While gross margin averaged 72.0 percent over the last three years, the firm's operating margin averaged -171.6 percent and net profit margin was -182.2 percent. This fact was also confirmed by managers who indicated that the cost of sending out one 22-meter boat to fish is CVE 40,000 per day, with personnel, ice, water, and bait comprising the bulk of expenses. Gross margin appears high because it excludes costs of fuel and certain other supplies from third parties, which are included in operating expenses. Further evidence of Pescave's weak profitability can be seen in its accounting return on equity (ROE), which averaged -14.1 percent and accounting return on assets, which averaged -12.1 percent.

As a fishing company, Pescave is moderately capital intensive, so cashflow analysis will add further insight into its operations. Adding depreciation back into net income, cash ROE is -5.9 percent and cash ROA is -5.1 percent. From this information, it is clear that Pescave's operating costs are too high.

Pescave's financial management leaves room for improvement. While, on the surface, the current ratio of 3.26 appears reasonable, most of the firm's current assets are tied up in accounts receivable. Most of these accounts receivable are due from local fishermen for boat rentals and repairs. Collections are weak, as days sales outstanding averaged 1,690 days between 1987 and 1989. According to management, the majority of these accounts are owed by individuals for boat rentals and repairs and may be difficult to collect. As a result of the delay in receivables, the company also lags its payments to suppliers: notes payable outstanding averaged 4,612 days over the last three years. Pescave's relative efficiency is poor, as can be seen by its fixed asset turnover of .11 and total asset turnover of .07.

The company's debt to total asset ratio averaged a modest 13.7% over the last three years. Management however, indicated that this ratio has risen sharply in 1990.

11. MAC

MAC's primary customers are EMPA, CTT, and the Bank of Cape Verde. Until recently, MAC both produced blocks and tiles for building and participated in the construction of buildings. However, because MAC does not have a license for civil construction, the firm can no longer bid on construction projects. Since construction accounted for 90.0 percent of sales in 1989, the most recent year for which financial information is available, MAC's exit from this business will certainly have a negative impact on its results.

The company now concentrates its efforts on producing blocks and hydraulic cement, called "pozolana." MAC currently produces 2,000 blocks per day. Management estimates capacity utilization of block production machinery to be 100 percent, however, MAC only operates one shift, so capacity utilization is less than 50 percent. Its capacity to produce roofing tiles is unused at present.

MAC currently has 168 employees. Staff break down as follows:

Directors	2
Technicians	2
Skilled workers	72
Unskilled workers	75
Office workers	9
Other workers	7
Apprentice	1
TOTAL	168

Many of the workers belong to the civil construction unit which no longer can engage in construction projects. As a result, according to management, the company could function with less than half its current number of employees.

MAC's profitability has been weak, with the exception of its gross margin which averages 55.0 percent. The firm's average operating margin is -7.0 percent and its average net profit margin is -5.9 percent showing high operating costs and inefficient financial management. Consequently, MAC's accounting ROA averages -12.1 percent, and its accounting ROE averages -16.3 percent. The standard deviations are significant, indicating that performance was highly variable for the period.

MAC is in the construction industry, so the firm is fairly capital intensive. It is therefore instructive to examine its cash returns. When depreciation is added back to net income, MAC's cash ROA rises to -.5 percent and its cash ROE rises to 8.8 percent. These ratios indicate that the underlying business is potentially profitable.

The management and efficiency ratios confirm that MAC is not optimally run. MAC's marketing management shows accounts receivable are collected in 354 days, or nearly one year.

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To counter this delay, MAC lags its payments with net purchases outstanding averaging 467 days. Inventory turns over 8.32 times per year which is only fair for a supplier of construction materials, but comparable to the market averages for Cape Verde. Fixed asset turnover of 3.63 times and total asset turnover of .67 times are low, indicating low utilization of assets.

12. TACV

TACV, the national airline, offers three different services: passenger transport, cargo service, and maintenance services offered to third parties. Passengers and cargo are transported internationally and domestically. The heaviest traffic, approximately 55 percent of the annual totals, is concentrated in the 18 weeks between June and September and during the Christmas season. TACV's typical international routes include flights between Sal and Lisbon, Paris, Amsterdam, and Boston as well as regional flights between Praia and Dakar. Of these routes, only the Praia-Dakar route is profitable. Domestically, regular service is offered between Praia, Mindelo, and Sal, with less frequent flights to the other islands. Domestic air transport historically has not been profitable, although recent changes in the tariff structure have brought revenues more into line with expenses.

TACV currently has a fleet of seven planes, which it plans to reduce to five within the coming year. Two planes are slated for retirement, one is to be sold, and one new plane is to be acquired, bringing the total to five. TACV uses its fleet for domestic and regional traffic. These planes have adequate capacity for passengers, but cargo space is constrained. International flights arriving in Sal have excess baggage which cannot be handled by the connecting domestic flights, therefore passengers are inconvenienced. For international flights, TACV leases planes from other carriers.

The airline's most significant costs are fuel and other third party costs and personnel expenses, accounting for roughly 75 and 17 percent of expenses respectively. Staffing levels are estimated by management to be 35 to 40 percent higher than needed to run an airline of this size.

The Summary Performance Table shows that TACV's profitability is generally poor, with the exception of gross margin. Average gross margin of 97.8 percent is high, but not particularly meaningful because airlines are a service industry, so goods are not manufactured for sale. A better measure of profit is its operating margin because it includes the large fixed costs component of operations. TACV's operating margin averages -13.8 percent, while its average net profit margin is -15.9 percent, indicating high operating costs and poor financial management. As a result, accounting ROA is -19.7 percent and the accounting ROE averages -103.7 percent. For these measures the standard deviations were very low, indicating these mean values have some explanatory properties.

Because the airline industry is capital intensive, it is instructive to analyze TACV's cash flow. When depreciation and leasing expenses are added back to net income, cash ROA of -9.5 percent and cash ROE of -55.8 percent are revealed. TACV's cash flow is insufficient to cover operating expenses before depreciation, indicating an ongoing need for capital infusions.

Liquidity measures are poor. Average liquidity is 0.82 times, a measure which has declined over the last few years, confirming that operations are draining cash from the firm. As a result, TACV lags payments to creditors with net purchases outstanding averaging 4,185 days. Days sales outstanding is much lower, averaging 82 days, which means that improving collections will cause only marginal improvements in the company's cash flow. TACV's other asset management ratios also demonstrate that the firm is inefficient. Average fixed asset turnover is 2.85 times while total asset turnover is 1.83 times, relatively low for an airline.

Debt averages 45.0 percent of assets; however, this figure belies the fact that debt rose to 66.0 percent of assets in 1990, showing that the firm has had to borrow money to deal with its cash flow problem. The interest earned ratio of -55.1 times is further evidence that TACV is in a difficult financial situation.

Mixed Enterprises

1. CABETUR

Cabetur sells travel and tourist services which include airline tickets, hotel reservations, car rentals, and related services, in addition to arranging tours. It is based in Praia, but also has an office in Sal. The company is in the process of opening a branch in Mindelo to increase its penetration of the Cape Verdean market and to provide better service to its customers. Because a large volume of its business involves Portugal, Cabetur is planning to form a joint venture with a Portuguese company to open a travel agency in Lisbon. Cabetur also would like to integrate vertically by building a resort hotel in Tarrafal.

In Cape Verde, Cabetur has three significant competitors, of whom Praiatur and Orbitur are the most well known. There are other small competitors in Praia and Mindelo offering day trips or island tours. Cabetur is perceived to be a strong force in the travel and tourism industry because of its focus on quality service. The company seeks feedback from customers to get ideas for service improvements. The fact that Cabetur uses computers in its operations also gives it a slight competitive advantage. Market share information is not available.

Cabetur has a small staff. The firm has one general manager and six employees in Praia, four staff members in Sal, and two in Mindelo. Staff is generally well-educated. At least one employee was trained for work in the tourist industry in Switzerland. Management takes time to explain the company's results to staff because employees participate in a profit-sharing plan. According to management, the profit-sharing plan is a strong incentive for employees.

Cabetur is a highly profitable company, as shown in its financial ratios. The firm's operating margin of 31.4 percent and net profit margin of 25.7 percent show that it is relatively efficient. Gross margin is not meaningful for a travel agency as services, rather than goods, are sold. Cabetur's accounting ROA of 11.5 percent and accounting ROE of 19.0 percent confirm that the company is very profitable.

Depreciation is a small portion of overall expenses at present. However, adding depreciation back to net income presents Cabetur's strong cash flow more accurately. The firm's cash ROA is 15.7 percent and cash ROE averages 25.8 percent.

Cabetur has strong liquidity as current assets average 1.66 times current liabilities. The fact that most of the company's current assets are tied up in accounts receivable though is of concern. Days sales outstanding average 263 days, which means that Cabetur could improve its financial management. Net purchases outstanding are not meaningful since a travel agency does not purchase goods for sale. Fixed asset turnover of 1.31 times and total asset turnover of .45 times indicate that Cabetur operations could be more efficient.

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Cabetur's debt ratio is low at 37%. Interest coverage is more than ample, as shown by the average of 165 times. The standard deviations for these values are high, implying that these values have to be interpreted with caution.

2. CABNAVE

Cabnave's first full year of operations was in 1984, when the international shipping market was in crisis. As a result, the company had a difficult time building its revenues. Over time, Cabnave's revenues have increased, but it faces stiff competition for ship repair services from places like the Canary Islands, and its capacity utilization is low. Indeed, the Canary Islands have a more elaborate infrastructure and can accommodate more ships than can Mindelo, giving the Spanish a strong competitive advantage in the naval repair business.
Cabnave's principal customers are Cape Verdean and Portuguese shipowners. Other important clients are Cuba, Bulgaria, the former Soviet Union, and Mauritania.

Cabnave uses installations owned by Cabmar, which it leases. This lease is an important element to address. From Cabnave's balance sheets and income statements, it appears that the firm has not made lease payments to Cabmar since at least 1985. These expenses have been capitalized as assets on the firm's balance sheets. An audit of the firm is needed to clarify exactly what the firm's true assets and liabilities are.

Staffing information was not available.

From the summary performance table, Cabnave's performance appears to be somewhat inefficient. It is likely that earnings are overstated since the firm has not made lease payments to Cabmar for several years. Average gross margin is 70.2 percent, indicating that the firm's cost of goods sold are well-managed. Cabnave's operating margin of 10.0 percent and net profit margin of 8.6 percent show that the company's operating expenses are high, resulting in lower profitability. In particular, personnel expenses comprise roughly 30 percent of costs. Services and supplies from third parties, which would include utilities, account for roughly another 30 percent of expenses. Cabnave's accounting ROA is 3.3 percent while its accounting ROE is 33.3 percent.

A cash flow analysis shows the firm's cash ROA of 4.5 percent and cash ROE of 47.0 percent. These numbers should be used with caution as they exclude the lease payment to Cabmar, which would pose a drain on cash flow.

Liquidity is reasonable as current assets are 1.42 times current liabilities. The asset management ratios show that Cabnave is inefficient. Inventory turnover is 3.58 times and total asset turnover is .38 times implying that capacity utilization is low. Fixed asset turnover ratio is not meaningful and, at 23.31 times, is misleading, as Cabnave does not own its installations, but rather leases them from Cabmar. Financial and marketing management is weak, but has improved over the last few years. Clients take an average of 167 days to pay their bills, while Cabnave takes an average of 338 days to pay its suppliers.

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The significance of the obligation to Cabmar is evident in Cabnave's debt to total asset ratio of 89.4 percent. Slightly more than three-quarters of the firm's debt is owed to Cabmar. The average times-interest earned measure of 5.74 has to be viewed with caution in light of its high standard deviation which could predict future problems with interest payments.

3. FAMA

Fama produces and packages pasta for sale in Cape Verde. The firm concentrates production on "short pasta", rather than making "long pasta" such as spaghetti. Fama faces tough competition from international producers whose pasta is exported to Cape Verde. Market share information was not available. Prices are regulated by the Government of Cape Verde.

Fama has the capacity to produce 1,000 tons annually. Current production is 250 tons per year. Production costs are half of the total costs. Fama's principal suppliers include the SOEs Moave and Electra.

Fama has 26 employees broken down as follows:

Directors	2
Administrative staff	10
Production workers	14
TOTAL	26

Staff levels are high for current activity levels.

Fama has not been profitable for the last three years, as shown on the summary performance table. While Fama's gross margin of 69.8 percent indicates that sales and costs of goods sold are reasonable, the firm's operating margin of .3 percent and net profit margin of -38.7 percent are weak. These reflect the need for lower operating costs as well as improved financial management. Fama accounting ROA and ROE are also negative and reflect losses incurred; they average -8.3 percent and -103.7 percent respectively. Because of these continued losses, equity is close to depletion. Low equity distorts the ROE measures, thus it is important to focus primarily on the ROA. It is important to note the relatively high standard deviations which indicate that these results have to be examined carefully and in conjunction with other ratios.

Fama incurs substantial depreciation expenses, so cash flow analysis will present a more reliable picture of operations. The Cash ROA is -1.1 percent and confirms that Fama's financial situation is troubled.

The liquidity and efficiency measures paint a similar picture. The firm has limited room to improve its cash flow without increasing sales, as clients tend to pay Fama within two months. The firm takes 641 days on average to pay its suppliers. This payment period has grown sharply over the last two years as Fama's ability to meet its obligations has deteriorated due to continued losses. Its current ratio is 0.40 times, reflecting low liquidity. Fama's asset management ratios point to inefficient operations. Inventory turns over only 5.20 times per year. Fixed asset turnover of .27 times and total asset turnover of .23 times confirm that capacity is underutilized.

It is not surprising that debt amounts to 90.9 percent of total assets. Times interest earned is a barely positive .01 which means that Fama is hardly able to pay its interest. Financing expenses should be higher, however, based on the firm's balance sheets and conversations with management. Fama has not met all its obligations to the Bank of Cape Verde.

4. HOTELMAR

Hotelmar owns and operates two hotels: Hotel Praia Mar in Praia and Hotel Xaguate in Fogo. The Praia Mar, which has 59 rooms and an average occupancy rate of 65 to 85 percent, is in a prime oceanside location. The hotel has a pool. Its tennis court is not functional, but could be rehabilitated. The restaurant, bar, and poolside bar all are nicely located. However, the quality of food and service need to be improved. Investment is needed in maintenance and infrastructure to improve the kitchen, restaurant, and poolside bar services. The restaurant could generate significant revenues if it had an excellent menu. The Praia Mar has 91 employees, including one director, reception staff, restaurant staff, laundry staff, and maintenance workers. This level of staff is high for a hotel of 59 rooms. Management at the Praia Mar has limited authority, because most decisions are taken by the hotel's board. As a result, the hotel eventually tends to lose its more entrepreneurial staff.

The Hotel Xaguate in Fogo has 19 rooms. Its occupancy rates tend to be lower, averaging 25 to 30 percent. The Xaguate has 11 employees. Little additional information was available on this hotel.

As mentioned above, the board of Hotelmar makes many operating decisions for the hotels. This management structure impedes efficient operations. The board consists of four members: two appointed by the GOCV and 2 elected by shareholders. Hotelmar has 11 additional staff members engaged in accounting and other administrative operations.

Hotelmar is heavily burdened by debt. According to management, cost overruns during hotel construction are responsible for the large debt to the Bank of Cape Verde. Construction costs were projected to be CVE 80 million, but were CVE 189 million when construction was completed. The firm recently renegotiated its debt with the bank.

Hotelmar is not profitable, as can be seen in the summary performance table. Although Hotelmar's gross margin averages 81.2 percent, it is not indicative because supplies typically are a small portion of a hotel's expenses. Its operating margin is 4.3 percent and its net profit margin is -8.0 percent. These measures indicate that Hotelmar has strong sales volume, but that its cost structure is too high. Personnel expenses, utilities and related costs, depreciation, and interest expenses are major components of Hotelmar's costs. Hotelmar's returns also demonstrate its weak performance: accounting ROA is -3.5 percent and accounting ROE is -

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156.6 percent. Equity has decreased sharply over the last two years due to losses sustained by Hotelmar, making its equity returns less meaningful.

It is also important to examine cash flow since depreciation comprises a large portion of expenses. Cash ROA is 3.8 percent, indicating the firm has sufficient cash to cover its expenses, even though its net income is negative. Cash ROE of 95.2 percent is distorted due to the low level of equity remaining with the firm.

Hotelmar's liquidity and efficiency measures also show that the firm is not efficient. Days sales outstanding average 144 days meaning clients take nearly five months to settle their accounts. Since accounts receivable comprise over 60 percent of current assets, the firm has less liquidity than its current ratio of 1.47 times would seem to indicate. Hotelmar takes 317 days on average to pay its suppliers because of its financial difficulties. Fixed asset turnover is .64 times and total asset turnover is .44 times. These ratios appear to indicate low utilization of facilities, but as indicated above, occupancy rates have been relatively high. The implication is that assets may be overvalued.

Because equity has decreased, the firm's debt ratio has grown over the years, averaging 95.5 percent. Hotelmar is barely able to manage its debt burden as shown by the times interest earned average of .28 times.

5. MORABEZA

Morabeza has three main product lines: shirts, trousers, and jeans. The firm operates only one shift daily for approximately eleven months of the year. Morabeza's primary clients are in Holland, France, and Portugal. Some of these clients supply their own raw materials for garment production.

Competition in the clothing industry is intense, particularly from Asian countries with lower operating costs. In contrast with competitors in Sri Lanka and China, Morabeza must import its raw materials, thereby raising its costs of goods sold and transport expenses. The industry also faces limits due to the Multi-Fiber Agreement among developed countries which reserves markets for existing competitors, making it difficult for companies to break into new markets.

Wages and salaries are Morabeza's single biggest expense. Morabeza has 110 employees, of whom 16 are in administration. The remaining staff work in production. Given the firm's poor operating margins, which are discussed below, Morabeza appears to be overstaffed.

Another major category of expenses for Morabeza is transportation. Because of irregular shipping schedules, Morabeza at times must resort to air freight in order to make on-time deliveries to clients, which raises transport costs.

Morabeza's gross margins, averaging 48.8 percent, have been consistently strong, indicating reasonable sales volume and raw materials sourcing. However, operating efficiency is weak.

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The firm has suffered persistent losses as can be seen in its average operating margin of -36.0 percent and average net profit margin of -54.4 percent. As a result, accounting ROA is -23.8 percent. In 1990, the firm's equity became negative, distorting the accounting and cash ROEs. However, for the previous two years, the accounting ROE averaged -47.0 percent.

Because Morabeza is not capital intensive, the cash ROA and ROEs do not reveal much about the firm's operations.

Financial management at Morabeza is relatively inefficient. Although liquidity has been reasonable with a current ratio of 1.43 times, its marketing management performance has been mixed. Days sales outstanding have averaged 59.3 days between 1988 and 1990, while net purchases outstanding have averaged 50.7 days, which represents fairly balanced management. The firm has managed its purchases in part by converting raw materials supplied by clients into finished goods, reducing the need for cash. Inventory turnover of .71 times is low for a clothing manufacturer, as is total asset turnover at .49 times.

Times interest earned is -3.59 times. Debt has averaged 92.9% of assets over the last three years although the recent debt swap will reduce this ratio.

6. SITA

Sita produces decorative paints and varnishes for sale in Cape Verde. The market tends to grow with the civil construction market, which has been increasing about 8 percent annually. Paint prices are regulated by the GOCV. The firm has little competition at present, but 30 percent of the paint market is to be opened to competition next year. The GOCV will allow competition to enter in three phases. Sita expects paint prices to fall and a decline in market share to occur as a result.

Sita has a capacity to produce 700 tons of paint annually. Current capacity utilization is estimated to be 65 percent. The company utilizes technology from the Portuguese firm, CIN, for which it makes royalty payments of a fixed percent of sales. Sita obtains raw materials from Holland and Portugal. Packaging is an important component of costs, accounting for as much as 20 percent of the finished product cost.

Sita has 27 employees. Sita has one general manager, eight to ten factory workers, and five security guards. The remaining workers are administrative, commercial, and management staff. The general manager makes day to day operating decisions. The board makes strategic decisions. Staffing levels are a little on the high side for the current operations.
Sita is a comparatively well managed firm, as can be seen on the summary performance table. Sita has a gross margin of 36.6 percent indicating reasonable sales and materials costs. The firm's operating margin of 9.2 percent and net profit margin of 6.6 percent reveal that operations could be more efficient. Sita's profitability is also reflected in its accounting ROA of 5.5 percent and accounting ROE of 14.0 percent.

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The paint industry has a substantial investment in facilities and productive equipment, so depreciation is a significant expense. As a result, the firm's cash flow presents a more realistic picture of the firm's operations. Sita's cash ROA is 10.0 percent and its cash ROE is 25.3 percent, revealing a healthy cash flow. All standard deviations are very low, indicating that these ratios are fairly indicative.

Liquidity measures are also satisfactory. The firm is fairly liquid, with current assets roughly equal to current liabilities. Financial and marketing management are reasonable. The firm collects from its customers in 25 days and pays its suppliers within ten days, on average. However, Sita's asset management and efficiency measures leave room for improvement. Inventory turnover of 1.73 times is low. Total asset turnover of .86 and fixed asset turnover of 5.09 times point to unutilized capacity.

Sita has a manageable debt burden, with debt comprising 60.8 percent of total assets. The times-interest earned of 19.36 is satisfactory.

TABLE IIIA1

COMPARATIVE CHARACTERISTICS OF WHOLLY-OWNED STATE ENTERPRISES

		ARCA VERDE *	CTT ●	ELECTRA *	EMPA ●	EMPROFAC *	ENACOL ●	[illegible] *	FAP *
Percentage of State Ownership		100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
LIQUIDITY:									
Current ratio (X)	Current A/Cur. L	0.42	1.54	1.98	1.32	2.41	0.93	1.78	1.88
ASSET MANAGEMENT AND EFFICIENCY:									
Inventory turnover (X)	Sales/Inventory	49.25	96.08	7.23	2.56	2.85	4.36	4.18	3.60
Days sales outstanding (days)	Receivables/ Sales/360	191.67	224.08	194.32	27.77	67.82	148.94	34.31	138.73
Net purchases outstanding (days)	Payables/Cost of Goods Sold/360	245.33	NA @@	199.04	130.68	8.86	128.31	29.88	61.00
Fixed asset turnover (X)	Sales/Fixed Assets	0.48	0.55	0.34	5.25	8.34	3.04	1.58	7.00
Total asset turnover (X)	Sales/Total Assets	0.33	0.38	0.27	1.28	1.10	0.91	0.89	1.19
DEBT MANAGEMENT:									
Debt to total assets	Total Debt/Total Assets	50.7%	63.0%	24.5%	70.7%	42.4%	89.3%	39.9%	82.9%
Times interest earned	EBIT/Interest Expense	-6.17	2.65	6.94	19.03	306.87	0.08	8.74	-3.46
PROFITABILITY:									
Gross margin	Gross Profit/Sales	83.1%	99.0%	54.7%	23.7%	39.9%	30.7%	41.6%	28.0%
Operating margin	EBIT/Sales	-38.5%	17.5%	7.2%	7.0%	12.5%	0.4%	8.3%	-5.9%
Net profit margin	Net Income/Sales	-46.6%	8.5%	6.0%	3.7%	6.3%	-6.2%	0.4%	-5.7%
Accounting return on assets (ROA)	Net Income/Total Assets	-15.5%	2.8%	1.6%	4.7%	7.5%	-5.3%	0.2%	-7.3%
Cash ROA	Net Cash Flow/Total Assets	-1.3%	17.8%	6.9%	6.7%	10.4%	-1.8%	6.7%	-3.2%
Accounting return on equity (ROE)	Net Income/Total Equity	-33.1%	6.5%	2.1%	15.6%	13.1%	-616.1%	0.3%	-80.1%
Cash ROE	Net Cash Flow/Total Equity	-3.3%	35.1%	9.1%	22.6%	18.1%	-379.0%	11.1%	-57.0%

* From unaudited financial statements.
● Data includes audited and unaudited financial statements.
\# Only one year of data available.
** Travel agencies have little inventory, so ratio is not meaningful and is excluded from group calculations.
\#\# Both equity and net income are negative, so numbers are not meaningful and are excluded from the group calculations.
@@ CTT has such a low cost of goods sold (99% gross margin) that the net purchases outstanding is not a meaningful ratio.

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TABLE IIIA2

COMPARATIVE CHARACTERISTICS OF WHOLLY-OWNED STATE ENTERPRISES

		INTERBASE @	MAC *	FESCAVE @	TACV @	GROUP Mean	GROUP Std. Error
Percentage of State Ownership		100.0%	100.0%	100.0%	100.0%		
LIQUIDITY:							
Current ratio (X)	Current A/Cur. L	6.24	1.09	3.28	0.82	1.97	1.48
ASSET MANAGEMENT AND EFFICIENCY:							
Inventory turnover (X)	Sales/Inventory	4.03	8.32	0.84	15.87	18.60	27.09
Days sales outstanding (days)	Receivables/ Sales/360	368.82	364.09	1,690.34	82.27	292.68	434.15
Net purchases outstanding (days)	Payables/Cost of Goods Sold/360	144.48	487.84	4,612.75	4,185.50	929.16	1,843.08
Fixed asset turnover (X)	Sales/Fixed Assets	1.36	3.63	0.11	2.85	2.71	2.31
Total asset turnover (X)	Sales/Total Assets	0.60	0.67	0.07	1.23	0.74	0.40
DEBT MANAGEMENT:							
Debt to total assets	Total Debt/Total Assets	16.7%	74.3%	13.7%	45.0%	51.1%	24.3%
Times interest earned	EBIT/Interest Expense	6.25	-9.33	-31.84	-54.08	20.56	88.04
PROFITABILITY:							
Gross margin	Gross Profit/Sales	56.4%	66.0%	72.0%	97.8%	56.7%	25.2%
Operating margin	EBIT/Sales	6.5%	-7.0%	-171.6%	-13.8%	-16.0%	48.3%
Net profit margin	Net Income/Sales	-2.8%	-6.9%	-182.2%	-15.9%	-20.2%	50.8%
Accounting return on assets (ROA)	Net Income/Total Assets	2.3%	-4.1%	-12.1%	-19.7%	-3.7%	8.2%
Cash ROA	Net Cash Flow/Total Assets	5.9%	-0.5%	-6.1%	-9.5%	2.8%	7.3%
Accounting return on equity (ROE)	Net Income/Total Equity	2.3%	-16.3%	-14.1%	-103.7%	-69.4%	189.0%
Cash ROE	Net Cash Flow/Total Equity	6.6%	8.8%	-5.9%	-55.8%	-32.5%	107.9%

* From unaudited financial statements.
@ Data includes audited and unaudited financial statements.
# Only one year of data available.
** Travel agencies have little inventory, so ratio is not meaningful and is excluded from group calculations.
Both equity and net income are negative, so numbers are not meaningful and are excluded from the group calculations.
@@ CTT has such a low cost of goods sold (99% gross margin) that the net purchases outstanding is not a meaningful ratio.

TABLE IIIB

COMPARATIVE CHARACTERISTICS OF MIXED ENTERPRISES

		CABNAVE	HOTELMAR	CABETUR	MORABEZA	FAMA	SITA	GROUP Mean	GROUP Std. Dev.
Percentage of State Ownership		87.8%	51.0%	30.0%	28.8%	20.0%	20.0%		
LIQUIDITY:									
Current ratio (X)	Current A/Cur. L	1.42	1.47	1.66	1.43	0.40	1.07	1.24	0.41
ASSET MANAGEMENT AND EFFICIENCY:									
Inventory turnover (X)	Sales/Inventory	2.58	24.02	1,475.64 **	0.71	5.20	1.73	7.06	8.82
Days sales outstanding (days)	Receivables/ Sales/360	168.72	143.73	283.41	59.27	59.50	25.21	119.84	81.29
Net purchases outstanding (days)	Payables/Cost of Goods Sold/360	336.51	316.54	NA	50.08	640.59	9.88	271.20	228.06
Fixed asset turnover (X)	Sales/Fixed Assets	23.31	0.64	1.31	2.20	0.27	5.09	5.47	8.13
Total asset turnover (X)	Sales/Total Assets	0.38	0.44	0.45	0.49	0.23	0.86	0.48	0.19
DEBT MANAGEMENT:									
Debt to total assets	Total Debt/Total Assets	89.4%	96.5%	37.0%	92.9%	90.9%	60.8%	77.8%	21.6%
Times interest earned	EBIT/Interest Expense	5.74	0.28	165.85	-3.50	0.01	19.36	31.28	60.63
PROFITABILITY:									
Gross margin	Gross Profit/Sales	70.2%	81.2%	99.7%	48.8%	69.3%	36.6%	67.7%	20.6%
Operating margin	EBIT/Sales	10.0%	4.3%	31.4%	-36.0%	0.3%	9.2%	3.2%	20.1%
Net profit margin	Net Income/Sales	8.0%	-8.0%	25.7%	-54.4%	-38.7%	6.6%	-10.0%	28.0%
Accounting return on assets (ROA)	Net Income/Total Assets	3.3%	-3.5%	11.5%	-23.8%	-8.3%	5.5%	-2.6%	11.4%
Cash ROA	Net Cash Flow/Total Assets	4.5%	3.8%	15.7%	-20.6%	-1.1%	10.0%	2.1%	11.4%
Accounting return on equity (ROE)	Net Income/Total Equity	33.3%	-158.6%	19.0%	-47.0%	-103.7%	14.0%	-40.2%	70.1%
Cash ROE	Net Cash Flow/Total Equity	47.0%	95.2%	25.8%	-33.7%	-5.6%	25.3%	25.7%	40.4%

* From unaudited financial statements.
● Data includes audited and unaudited financial statements.
Only one year of data available.
** Travel agencies have little inventory, so ratio is not meaningful and is excluded from group calculations.
Both equity and net income are negative, so numbers are not meaningful and are excluded from the group calculations.
@@ CTT has such a low cost of goods sold (99% gross margin) that the net purchases outstanding is not a meaningful ratio.

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TABLE IIIC

COMPARATIVE CHARACTERISTICS OF PRIVATE ENTERPRISES

		ALUPLAST #	SHELL	SODAL	GROUP Mean	GROUP Std. Error
Percentage of State Ownership		0.0%	0.0%	0.0%		
LIQUIDITY:						
Current ratio (X)	Current A/Cur. L	2.48	2.10	0.89	1.82	0.88
ASSET MANAGEMENT AND EFFICIENCY:						
Inventory turnover (X)	Sales/Inventory	3.31	4.48	1.24	3.01	1.34
Days sales outstanding (days)	Receivables/ Sales/360	180.80	62.21	112.98	118.66	48.58
Net purchases outstanding (days)	Payables/Cost of Goods Sold/360	36.57	69.80	212.63	106.33	76.38
Fixed asset turnover (X)	Sales/Fixed Assets	3.61	4.59	3.78	3.99	0.43
Total asset turnover (X)	Sales/Total Assets	0.70	1.49	0.71	0.97	0.37
DEBT MANAGEMENT:						
Debt to total assets	Total Debt/Total Assets	32.4%	60.2%	118.6%	70.4%	35.9%
Times interest earned	EBIT/Interest Expense •	1,738.71	66.31	-2.68 •	600.81	805.11
PROFITABILITY:						
Gross margin	Gross Profit/Sales	66.6%	33.0%	32.8%	44.1%	15.8%
Operating margin	EBIT/Sales	24.8%	4.8%	-21.6%	2.7%	19.0%
Net profit margin	Net Income/Sales	16.2%	2.9%	-41.8%	-7.6%	24.7%
Accounting return on assets (ROA)	Net Income/Total Assets	11.4%	4.6%	-30.1%	-4.7%	18.2%
Cash ROA	Net Cash Flow/Total Assets	19.0%	9.7%	-28.6%	0.7%	18.7%
Accounting return on equity (ROE)	Net Income/Total Equity	16.9%	10.7%	NA ##	13.8%	3.1%
Cash ROE	Net Cash Flow/Total Equity	28.0%	23.8%	NA ##	25.9%	2.1%

* From unaudited financial statements.

● Data includes audited and unaudited financial statements.

\# Only one year of data available.

** Travel agencies have little inventory, so ratio is not meaningful and is excluded from group calculations.

\#\# Both equity and net income are negative, so numbers are not meaningful and are excluded from the group calculations.

●● CTT has such a low cost of goods sold (99% gross margin) that the net purchases outstanding is not a meaningful ratio.

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