FIELD REPORT

Privatization Strategies and Techniques: Instituting Practical Methodologies

May 10 - 28, 1993

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Training Workshop Report

Lusaka, Zambia

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Center for Financial Engineering in Development

CFED
Center for Financial Engineering in Development

June 1993

Mr. Val Mahan
Project Officer
U.S. Agency for International Development
Lusaka, Zambia

Dear Mr. Mahan:

The Center for Financial Engineering in Development (CFED) is pleased to submit this final Training Workshop Report on the "Privatization Strategies and Techniques: Instituting Practical Methodologies" training programs held in Zambia May 10 - 28, 1993 (contract number 623-0463-C-00-3018-00).

We have included sections on the program itself, a cross-comparison of the participants in attendance, a "lessons-learned" section, and recommendations for future training in both privatization and organizational management issues.

CFED would like to take this opportunity to thank those individuals and institutions who helped make this project a success. First, Mr. James Matale, Director of the Zambia Privatisation Agency for his unwavering support in the goals and objectives of the training exercises, Mr. Wilbur Jones and the staff of the Human Resource Development Project, who were responsible for overall participant recruitment and excellent administrative support, Mr. Maxwell of ZACCI, who provided excellent on-site administrative management support during the workshops, and finally, to Ms. Betty Wilkinson and the staff of USAID who provided the training team with all the necessary support to effectively complete our project and make our stay in Zambia as welcomed and comfortable as possible.

On behalf of the training team, we thank you again for the opportunity of working with the USAID/Lusaka Mission and the Zambia Privatisation Agency on this important project and we looking forward to an opportunity of working with you again in the near future.

Sincerely,

Tommy White

Tommy White
Director of Special Projects

U.S. Main Office
1255 23rd Street, N.W., Suite 870, Washington, D.C. 20037
Telephone (202) 728-2983 Facsimile (202) 728-1865 Telex 3737669 CFED

Field Offices
Santiago, Chile • Warsaw, Poland • Colombo, Sri Lanka • Santo Domingo, Dominican Republic

Privatization Strategies and Techniques: Instituting Practical Methodologies

Training Workshop Report

June, 1993

I. Introduction

The Center for Financial Engineering in Development was retained by the U.S. Agency for International Development/Lusaka and the Zambia Privatisation Agency to conduct a series of training workshops on "Privatization Strategies and Techniques: Instituting Practical Methodologies." These training programs, carried out in the time period of May 10 - June 1, 1993 and held in Zambia, included the following:

> A One-Day Workshop (May 13, 1993) for board members of the Zambia Privatisation Agency;
>
> Two Five-Day Workshops (May 17-21 and May 24-28, 1993) for staff members of ZPA, line ministries, the media, and other invited guests.

The workshop trainers for these training exercises were the following:

Mr. Clare Humphrey
Dr. Rolf Luders
Mr. James Ryan
Mr. Tommy White

The general timeframe and scope of the project included the following:

1. Week One (May 10-15)

During the first week of the assignment, the workshop trainers held meetings with staff and management of ZPA, USAID, HRDP, and ZACCI to discuss the general focus of the training exercises as well as to develop further the actual training program schedule. These meetings were very fruitful for the trainers, in as it provided an opportunity to place the international experiences of the instructors into the Zambian political, economic, and social context. It also allowed the trainers an opportunity to make meaningful changes to the actual training programs which allowed for a more appropriate connection into the Zambian privatization program. This time period also provided the trainers an opportunity to caucus more frequently on the program schedule, something that might not occurred as easily without the preliminary week in Lusaka.

Also during the first week, the one-day meeting with the members of the Board of the Zambia Privatisation Agency took place (May 13, 1993). Dr. Rolf Luders was the guest presenter at this meeting. The purpose of this program was twofold. First, to discuss the Chilean privatization program and its ramifications for Zambia and second, to provide insight to the Board on their roles and responsibilities in their decision-making capacity vis a vis the Zambia Privatisation Agency. Both objectives were achieved in the discussions and we believe the Board has a better understanding of their roles and responsibilities. Unfortunately, however, only six of the board members attended the meeting (out of eleven) and thus the full impact of Dr. Luders insights will most likely not be felt.

2. Week Two (May 17-21) and Three (May 24-28)

During these one week periods, each of the five-day workshops was held at a training facility in Siavonga. For the first program, 23 participants were in attendance (10 from ZPA, 8 from ministries/agencies, and 5 from the media). For the second program, 25 participants were in attendance (14 from ZPA, 7 from ministries/agencies, and 4 from the media).

The training was conducted by Clare Humphrey, Jim Ryan, and Tommy White. The training methodology included a mixture of lecture, class discussion, small group case analyses, and a negotiation privatization simulation exercise. Attached are copies of the faculty materials and case/simulation exercises distributed to the participants. Additional materials were also utilized, including flip chart items and hand written overhead transparencies to conduct the training sessions. Our goal as the trainers of the program was to deliver a high quality training experience on the strategies and methodologies of privatization and their appropriate uses to the Zambia privatization program. Our objective was to provide a "confidence-building" opportunity and foundation for those involved in privatization process through our instructional learning processes.

We believe these goals and objectives were met in the training exercises. Our own informal feedback from the participants as well as the formal evaluations conducted by the Human Resource Development Program confirm this. One general issue raised by almost all the participants was the desire for a longer program (something, we have learned, that all Zambia participants request). However, from our viewpoint, we concur. A program of seven days in length would have been more appropriate. We had quite a lot of material to cover and at times we had to either rush through materials or leave out important information.

The following sections will outline further the participants, a comparison of the two groups, the key issues/lessons generated by the participants in the discussions, and recommendations for future action. In the Annex is a copy of the original program schedule.

II. Participants

Participants in the privatization workshops included ZPA staff members, representatives from line ministries and other government agencies, and members of the media. Each of the groups had motivations and goals in attending the programs, and they could, therefore, be expected to benefit differently from their participation.

For both sessions, media participation was limited to the entire Monday session and approximately one-half of the Tuesday session. For this reason, their experience and knowledge gained from the sessions would be different from that of the other participants. As a practical matter, throughout the workshops, no distinction was made between ZPA staff members and representatives of the line ministries and government agencies.

1. ZPA Staff

The ZPA staff was generally a younger and somewhat less experienced group as compared to the other participants. They generally had good educational backgrounds and were capable of maintaining the pace of the training. They had clear motivations in participating, as they were seeking direction and specific skills that would help them better perform their tasks at ZPA.

Initially it appeared that ZPA staff members were less confident than the other participants in their privatization skills. This resulted in their contributing less to discussions in the early part of each week. However, as each week progressed, ZPA participants gained confidence and contributed to all discussions on a more equal basis. Their insight to the critical issues also improved as each week progressed.

The following are the benefits derived by ZPA staff members from their participation in the workshops:

i. A better understanding of policy implementation issues and the purposes of privatization;

ii. Attainment of knowledge and new skills in a variety of privatization strategies and methodologies that can be applied directly in the execution of their functions at ZPA;

iii. Increased confidence in their abilities to handle their tasks at ZPA;

iv. Increased comraderie and spirit of teamwork within ZPA.

2. Ministry/Government Agency Staff

In general, these individuals were more experienced in privatization understanding than the ZPA staff. The motivation of the Ministry and Agency staff in attending was not as clear as the ZPA staff, however, it was recognized early on in each workshop the important roles these organizations must have in the privatization process. Interest in all aspects of the Zambia privatization process was high, and it appeared that the Ministry/Agency participants had an interest in the materials beyond the scope of their own roles in the privatization program.

The following are positive results of their participation in the workshops:

i. An increased understanding of policy issues and economic purpose/benefits of privatization;

ii. A furthering of understanding of the role of ministries/agencies in privatization and how they must participate to make the program a success;

iii. An increase in the awareness of the need for cooperation and integration between ZPA and other government agencies.

3. Media Representatives

Participants also included representatives from the broadcast and print media. Most are specialists in reporting on economic and business matters in Zambia. The primary purposes in attending the programs were to report on the workshop and to gain knowledge that would help in covering future events related to the privatization program.

Since the media participation was limited to the first two days, the participants were not involved with case studies or the work in small groups. Many of the media participated actively during the presentation of basic materials while other maintained a more passive role.

The following benefits were derived from workshop participation:

i. Attained a foundation of knowledge in the purpose, policy, and implementation of privatization;

ii. Gained privatization knowledge that will be useful in reporting on privatization issues and events;

iii. Learned how to recognize rumor and misinformation which often occurs in a privatization program;

iv. Gained valuable contacts with those involved with the privatization process.

III. Comparison of the Two Training Programs (May 17-21 {Group 1} and May 24-28 {Group 2})

In comparing the two training groups, there are several elements in the group dynamics that played a role in the implementation of the training. It was the trainers original intent to offer the same program twice, however, adjustments were made between the two programs as well as during the second program, as it became evident that with different participant backgrounds, it was important to adjust the program content somewhat to reflect those changes in the participant dynamics.

In a general statement on the two groups, we were particularly pleased by the participant "inquisitiveness" throughout the workshops, and in each case, the trainers could see a real learning curve being generated, especially when the discussion focused on case studies and the simulation exercise and the participants had an opportunity to apply what they had learned in previous sessions.

In specific comparisons of the two groups, there were several differences that highlighted each group. For example, the trainers felt that the Group 1 participants were not active in the early class discussions, and it was not until the middle of the second day that they overcame their "shyness" and began to join the debate more actively. We concluded this was most likely due to the attendance of senior members of ZPA, which caused a reluctance on the part of the participants to speak up. In Group 2, this was not the case, as the participants from the beginning were very active in the discussions.

However, the trainers felt the overall understanding of the privatization process/methodologies for Group 1 concluded at a higher level (eg that the participants were more intellectually attuned to the privatization issues) than for Group 2. This was evident early on in Group 2's program when participant presentations were made for the Textile Mills Case Analysis. The participant presentations were flat as well as elementary in their analysis, an indication that the level of privatization comprehension was not as high. The trainers made the appropriate adjustments, not by lowering the level of the presentations, however, but rather by challenging the participants to work harder in their future analyses. Although the second case analysis (Nepal Tea Development Corporation) was again not as thorough or as creative as Group 1, there was a definite improvement in the analyses.

A final area of difference between the two groups includes the approach and analysis of the Cula Privatization Simulation Negotiation Exercise. The Cula Simulation Exercise consisted of two bidder teams (one local buyer with 25% ownership in the SOE and one foreign investor buyer) and one government team. The objective of the exercise was for each group to develop a negotiation strategy for the privatization of the SOE based on certain parameters provided in the case as well as confidential information given to each team. Each bidder team went through a series of meetings with the Government team where bids were presented orally and discussion ensued. There was no declared "winner" in as the goal of the exercise was for each side to gain insightful information to the negotiation process as well as an appreciation of all of the information necessary to implement a successful privatization transaction.

In examining the two negotiation exercises, it was evident that Group 1's negotiation process was conducted at a higher level than Group 2's. The teams in Group 1 more accurately portrayed the roles of each by "thinking" like a foreign investor, or local investor, or the government. This in turn brought out quite successfully the biases that often go along with such a negotiation process. For Group 2, this was not as pronounced, however, the conclusions they reached did indicate a successful negotiation process.

The "lessons learned" from this role playing simulation exercise include the following four, as applicable to Zambia:

1. The Government of Zambia must identify and lobby early on the key players who will be involved with each privatization transaction. Knowing who will be affected by the particular privatization and which groups may most likely be obstacles is critical. These groups typically include labor, the media, the general public, the bureaucrats, and the managers, to name a few.

2. The Government of Zambia must determine early on the appropriate financial packaging acceptable to them. Although it was recognized that in Zambia's case privatization transactions are currently on a cash basis only, that for the larger and more complicated enterprises, this may not be the case and creative financing opportunities must be considered.

3. The appropriate terms of sale must be recognized, including the bidding process as well as an indication as to what are the government concerns and the buyer concerns for a particular transaction. Government concerns include business resources and integrity of the potential buyer while several buyer concerns include the freedom to make and repatriate profits, hire/fire, and manage the firm free from government interference.

4. The Government of Zambia (and, of course, the potential buyers for themselves) must develop an effective negotiation strategy that takes into account all the objectives and goals of the government. In the case of Zambia, a "win-win" negotiation strategy was considered desirable over a "win-lose" strategy because it was believed that privatization must be seen for its entire process and not as separate and individual transactions.

IV. Key Issues Generated and Discussed During the Training Sessions

Although keeping to a particular training schedule is important to a training program, often the discussions and resulting issues that arise "makes or breaks" the success of a program. We have listed below several items/themes which we believe captures the essence of much of the discussion/debate by the participants during the two workshops. The items listed are "participant-driven," meaning that these were the topical issues that either troubled participants or which they found the most important in implementing Zambia's privatization program. For each, we have listed the issue, provided a brief comment, and a response action on how the trainers handled the issue.

1. - Issue. The discussions indicated the conviction among the participants that for the privatization program to be a success, communication among the key players and agencies must be improved. Information, viewpoints, and understanding must be freely disbursed among the important sections and agencies involved in the privatization process. This applies not only to the various sections within ZPA, but also in the interrelationships with and among other agencies and ministries.

   Response. Throughout the presentations and discussions and, especially, during the case studies, the trainers constantly stressed the advantages of sharing information and insights when approaching issues and solving problems. The value of ZPA fostering teamwork was a prime feature of training methodology and content.

2. - Issue. There was universal admission that public awareness of the privatization program is abysmally low. Lack of knowledge and understanding has bred uneasiness, distrust, and opposition; and the success of the program can be seriously threatened. The participants were particularly aware of the need to challenge myths and misinformation. If the ZPA is to be the voice of the privatization program, a forceful, objective, and comprehensive public awareness/education campaign must be launched at the earliest possible moment so that the effort can be pre-emptive rather than responsive, proactive rather than reactive. Heretofore, the field has been left to the opposition.

   Response. The absolute necessity of designing and launching a comprehensive public awareness/education campaign aimed at the concerns of key target groups and to dispel myths of privatization was a constant theme throughout the workshop.

3. - Issue. Coordination and integration of the efforts of all key agencies involved in the privatization process must be improved. The function and objectives of the various important agencies must be better understood and integrated. Basic goals and program directions can only be achieved through conscientious application of teamwork approaches from early on in the process, with ZPA in the forefront of the implementation effort in order to overcome obstacles during the process and to avoid last minute surprises and problems when actual transaction negotiations commence.

   Response. Throughout the workshop, awareness of this factor was strengthened by use of examples and prototype solutions. Considerable stress was placed on development of policies and programs that are coherent, coordinated, comprehensive, and consistent.

4. - Issue. There was widespread recognition that the crucial and volatile labor issue (particularly the question of retrenchments) has not been faced squarely to date. This came up in virtually every session, no matter what the topic. It was agreed that special focus must be placed on developing various types of concrete packages to meet the legitimate concerns of labor. It was further recognized that this analysis and prescription must commence early on and continue throughout the process. There was general concern that this issue was not being addressed adequately for Tranche 2 privatizations.

   Response. Repeated examples of labor problems related to privatization in various countries were given, along with citation of programs and policies to confront such issues. The cost of inattention to labor issues was mentioned numerous times during the week.

5.- Issue. While there was general recognition on the importance of the relationship between privatization and private sector development and the need for public sector-private sector cooperation, it was obvious that a lack of knowledge and understanding of and experience with the private sector (at times bordering on hostility or at least latent distrust) still exists within the ranks of the ZPA and other government agencies responsible for designing and carrying out the privatization program.

Response. Numerous examples were cited to demonstrate the positive and negative ramifications of public sector-private sector relations and cooperation and their contribution or hindrance to national economic progress in today's globalized economy. The benefits of the partnership approach in contrast to an adversarial relationships was constantly reiterated.

6. - Issue. The participants' fear of a recurrence of foreign domination, a heritage of a colonial past, surfaced frequently during discussions of foreign investment in connection with privatization of SOEs.

Response. The trainers cited examples of both the benefits and cautionary areas of foreign investment while showing how countries have developed strategies to face this issue. The teaching approach was pragmatic rather than ideological and attempted to separate myth, experience, and reality.

7. - Issue. It was evident that the participants did not have a well developed or clear picture of an overarching government policy framework for market-driven economic development in general and privatization in particular within which the ZPA needs to function. They did not appear to be certain just how and where policy was determined and disseminated or how the privatization implementation tasks of the ZPA were affected.

Response. Considerable stress in trainer presentations was placed on determining long-term goals and short-term objectives for privatization strategies and methodologies and how the policies and programs of various concerned agencies must be integrated.

8. - Issue. With regard to transaction negotiations, there appeared to be overwhelming dependence on cash payment as the mandated method for buyers purchasing SOEs. Inattention was given to the possible need for longer term payment schedules and for handling enterprise debt, both of which could become major factors in later tranches involving larger, more complex SOEs.

Response. While realizing the parameters of mandated practice on cash payment (the Privatization Act), the trainers raised warning flags in regard to privatization of larger enterprises down the line. Possible approaches of payment scheduling, debt forgiveness, and swaps to this and related questions were offered, along with citing the experience of other countries.

V. Recommendations for Further Training

It was evident at the conclusion of the program that further training in a variety of privatization related issues for the ZPA board and staff as well as for other key individuals/groups is critical for the successful implementation of Zambia's privatization program. This training can and should take many forms, in as the needs are varied and great for each of the three key target groups.

The most important item in this process is to devise a training implementation strategy as soon as possible, so as to take advantage of the momentum of the training just completed. By maintaining momentum, those who have just completed the workshops will gain confidence in using their new knowledge, on the premise that additional training will be made available in the future.

Based on our observations over the three week period and on our training experience, we recommend the following additional training for each key group:

1. ZPA Board Members:

As a follow-up to the one day workshop conducted by Dr. Rolf Luders, a series of workshop exercises, with the full board in attendance, should be enacted to build upon this knowledge base. In as the Board has the final say on implementing particular privatization transactions, their ability to synthesize detailed information and become a decision-making entity is critical to implementing privatization.

It was evident that at the conclusion of the one day workshop the Board currently is not exercising this authority. Through a series of one-two day programs, relevant privatization information can be disseminated to the Board, so as to provide them better with the confidence to enact appropriate decisions.

2. ZPA Staff:

For the Zambia Privatisation Agency staff a variety of future training will be important. We have included below four "tracks" for the implementation of additional training, each keying in on those issues most relevant for human resource development in ZPA. The tracks are meant to be carried out in an overlapping manner, so that the full benefit of the training can have the greatest impact soonest.

Track One: Specialized Departmental Training

Now that most, if not all, ZPA staff has had exposure to general privatization methodologies and experience, privatization specialty training should be considered in the next level of training. This should most likely be "compartmentalized," meaning that each department within ZPA should have specific training within their specific areas of responsibilities. For example, further training of the FEB Department is needed in financial statement analysis, business analysis, and valuation, as they relate to the privatization program.

We recommend that a specific training agenda be drawn up for each department (PA, FEB, Legal, Social Impact, and Marketing) within ZPA. We further recommend that each department plays a role in identifying their own training needs- the individuals within each department are well aware of their knowledge shortfalls and they are in the best position to identify their particular training needs. This approach may be a bit controversial, but at the very least consider a brainstorming session within each department for training ideas. Additionally, outside experts/facilitators could also be utilized to help direct the development of such program ideas.

It is difficult to recommend definitive lengths for such workshops, however, in examining each five day program just completed, we believe that the effective attention span for participants is approximately five to eight days. For programs that may need more classroom time (i.e. training in financial analysis) a better alternative may be to schedule the training over several weeks or even months (similar to a university schedule).

Track Two: Organizational and Management Training

A foundation has been developed for the different departments of ZPA to begin to work in a more organized and coordinated fashion. However, this initiative will be lost unless further training in operations and management and team-building skills are made a priority for ZPA staff.

"Organizational and Management" training has often been labeled "soft training" and is sometimes viewed as having little visible benefit to an organization. In the case of the ZPA, however, it will play a vital role because of the need to develop a corporate identity and culture amongst staff members, items that will be key as the Zambia Privatisation Agency has more and more of a visible role in the development of the Zambian economy.

The ZPA should be viewed as an "information processing" entity. Unless there is a well coordinated and planned process for both controlling and disseminating information, especially amongst the departments, problems will arise in the privatization implementation process. For the privatization program to proceed smoothly, coordinated and integrated communication channels are vital to its success.

We recommend a series of short organizational and management programs for the staff of the ZPA to overcome these potential pitfalls. By developing a sense of teamwork and relational-ship understanding, the ZPA will be better equipped to effectively carry out their projects in a more professional and timely fashion.

Track Three: Coordinated "On-The-Job" Training with the Consultants Currently in ZPA

Currently there are six expatriate consultants working within the ZPA on privatization implementation. These consultants, all experts in their respective fields of finance, marketing, social studies, and privatization have a wealth of information that can easily be transferred to the staff members of the ZPA.

Although these consultants have specific tasks to complete as a function of their scopes of work, providing time for a transfer of intellectual technology should be high on the list. A goal of the ZPA is to be as self-sustaining as possible and working with the expatriates is an excellent way to accelerate the process. We recommend the following two actions:

1. Have each department hold regular meetings with the appropriate consultant(s) to discuss progress to date as well as to brainstorm future privatization projects. These types of regular and open discussions (initiated by the ZPA staff - not by the consultants) are important for breaking down the cultural and information barriers. The ZPA staff members should be the ones directing the meetings.

2. Assign 1-3 staff members to each consultant in a "mentor" role so they can work with the staff members on a fully scheduled basis. The consultants may disagree with this arrangement (because in the short-run it is always easier to complete a project yourself rather than train someone to do it) but if it is explained to them that this training has as much priority as "completing the privatization task at hand" then resistance should be minimal.

It must be recognized that it is a very difficult, time consuming, and tiresome process to train people "on-the-job". A commitment to this plan of action must come from the senior officials of ZPA, because both the staff and the consultants must be committed to the implementation of the plan. If not, disillusionment will most likely occur and an even greater reliance on outside consultants will most likely be necessitated.

Track Four: Informal Exchanges Once a Week for 1-2 hours on a Specific Privatization Topic, Issue, or Event

Although technically not a "training" item, informal exchanges on a specific privatization topic/issue/event is an excellent way to keep the staff up-to-date on new privatization technologies. These exchanges could be ZPA-staff led or, on occasion, led by outside experts (especially as additional expatriate consultants will most likely be in Zambia on a variety privatization assignments).

All the participants expressed in interest in this type of forum of exchange and clearly felt the benefits of this activity would help in their planning and development.

3. Training for Other Zambian's:

A large majority of participants made an interesting comment on the need for training for a much larger audience, including members of Parliament, the media, line ministries, labor representatives, and financial institutions.

The justification for this is that as privatization (and private sector development) becomes more and more important to the economic development of Zambia, the broad-based support it will need is critical for its survival. Their comments focused on an illusive "glass ceiling" in the understanding of privatization issues by key decision-makers and their need to attend programs such as these for further enlightenment.

A typical statement can be made on the need to hold conferences, training workshops, press conferences, etc., which we all know is the means by which to voice privatization issues. However, what is more important is the message itself, who is saying it, and who the target audience is. The privatization "message" is a difficult concept to master, especially when most individuals equate privatization with negative images, i.e., job loss.

Therefore it is vitally important that the senior staff of ZPA devise a strategy on the most appropriate methodologies to "train" key officials, agencies, and the public at large on privatization: both its benefits and potential drawbacks. Currently, the opponents to privatization have been carrying the field- thus privatization has received in general poor press. If ZPA wants to build a constituency of supporters of privatization, they must begin as soon as possible, lest the opportunities to be aggressive in a privatization promotional campaign be squandered.

VI. Conclusion

As stated previously, the objective of this training exercise was to provide the participants with a solid background to privatization strategies and methodologies used worldwide. The completed training should be viewed as a springboard from which to develop the institutional capacity of the Zambia Privatisation Agency to implement the privatization program in Zambia. We feel confident that this objective was achieved. However, to receive the fullest benefit of the training it is imperative that follow-up, both in additional training as previously outlined as well as a coordinated effort to incorporate the ZPA staff into the privatization process, be implemented as soon as possible.

Training of any kind is only effective if it is put to practical use. Therefore, for ZPA to receive the greatest benefits, a strategic plan which outlines future obtainable goals and objectives in training and staff development should be enacted.

ANNEX

* Program Agenda
* Participant Lists
* Program Materials

PROGRAM AGENDA

Privatisations Strategies and Techniques: Instituting Practical Methodologies

Lusaka, Zambia

May 13, 1993

Rationale

A critical component for all privatisation programs is the development of key processing mechanisms to effectively implement privatisation. Most privatisation experts agree that one of the major causes of delayed or even failed privatisation programs in developing countries is that appropriate communication and dialogue between those responsible for overseeing privatisation and those actually implementing privatisation is not developed, i.e. that the "process" of how the privatisation will be carried out is not well defined. In cases when this has occurred, attempts to privatise have had less than satisfactory results and often privatisation does not occur at all. For privatisation to be successful, defining the roles and responsibilities, and more importantly, the relationships, amongst the key parties is needed for effective privatisation implementation.

Objectives

To examine these issues in-depth, a one-day seminar for the newly selected Board Members of the Zambia Privatisation Agency has been developed. The purpose of this seminar is to develop an understanding about privatisation processes and to develop an understanding of how the Board Members should effectively work with the Zambia Privatisation Agency in carrying out privatisation transactions.

By disseminating critical privatisation issues, this seminar will achieve three objectives. First, the seminar will provide a brief overview to privatisation and develop a framework for understanding how privatisation can be successfully implemented in the Zambian political and economic environment. Second, this seminar will further serve as an opportunity to facilitate the idea of consensus building amongst the Board Members and demonstrate the commitment of the Government of Zambia to a long-term and meaningful program of private sector-led economic growth. Third, this seminar will focus on the role of the Board and develop a clear sense of their responsibilities vis a vis those of their technical agency, using prior country experience (primarily Chile) as an opportunity to review and revise responses to technical input.

Program Topical Outline

I. Maintaining the Appropriate Institutional Framework for Privatization

* Political Support and Legislative Requirements: Sustaining Privatization Programs
* Economic, Social and Financial Implications of Privatization Implementation
* Case Study: The Chilean Privatization Model

II Privatization in Zambia: Developing a Cohesive and Transparent Strategy by the Board Members

* Importance of Continued High Level Support for Privatization
* Defining the Roles and Responsibilities of the Board Members vis a vis the Zambia Privatization Agency
* Determining Level's of Control and Trust in the Process
* Creating Team-Building and Consensus in Implementing Zambia's Privatization Program
* Understanding Bid Evaluations and Negotiations: The Necessity of a Transparent Strategy

Privatization Strategies and Techniques:

Instituting Practical Methodologies

May 17 - 21, 1993
May 24 - 28, 1993

Rationale

This training exercise will focus specifically on the strategies, techniques, and methodologies utilized for implementing successful privatization programs and transactions. To implement privatization successfully, the Zambia Privatisation Agency must be well versed on the concepts, techniques and methods of privatization. They must have a complete understanding of the strategies and techniques that determine success or failure from one transaction to the next. By thoroughly examining these topics and issues, a strategic plan of action can be formulated and integrated into the existing Zambian privatization framework and objectives.

Objectives

The objectives of this intensive training exercise are threefold. First, this workshop will provide the participants with an opportunity to develop a comprehensive understanding of the privatization process, from the strategic level through the actual transaction stage. A rigorous presentation of enterprise diagnosis, divestiture strategies and options, privatization marketing and financing, and transaction evaluation and monitoring will provide a solid basis from which to explore selected privatization topics in further depth. The key focus will be on implementing privatization.

Second, this workshop will provide an opportunity for participants to examine critically those aspects of privatization most relevant to the Zambian case, focusing on setting up systems and anticipating difficulties so as to improve problem-solving capacities. In this training exercise, an important issue for the participants will be to apply the techniques and methodologies presented in the program and begin formulating a privatization implementation strategy that will improve the functioning role of the Zambia Privatisation Agency vis a vis implementing actual privatization transactions.

The third objective of this workshop is for the program to develop a sense of team commitment and team building for those who will be responsible for privatization. By examining previous privatization endeavors (both external cases as well as the Zambia Trance One Privatizations), participants will be exposed to both the successes and failures of privatization in a variety of settings. Most importantly, having an opportunity to dissect problems that have plagued previous privatization programs and transactions will not only serve as a useful learning tool, but will give participants the confidence to address similar problems if and when they arise in Zambia.

3. Program Outline

Privatization Strategies and Techniques: Instituting Practical Methodologies

i. Determining the Framework for Successful Privatization Implementation

* Developing a Unit Privatization Strategy: Identifying Attainable Implementation Goals and Objectives
* Understanding Privatization Strategy: Analyzing the Political, Legal, Social, Financial, and Economic Bottlenecks
* Case Studies: Contrasting Two Country Approaches

ii. Diagnosis, Selection, and Valuation of Privatization Candidates

* "Inventorying" State-Owned Assets: Determining What the Government Owns
* Creating an Enterprise Database for Financial and Economic Analysis
* Developing an Effective Criteria Methodology for Privatization Determination (Retention, Restructure, or Privatize)
* Determining a Realistic Timetable for Privatization of Appropriate State-Owned Assets
* Readying an Enterprise for Privatization: Legal, Financial, and Rehabilitation Considerations
* Determining the Appropriate Value: Applications of Valuation Methodologies
* Case Study: Tranche One Privatizations

iii. Determining Future Ownership: Divestiture Techniques and Options

* Examining Divestiture Strategies and Options
* Enterprise Restructuring as Part of the Privatization Process: Whose Role?
* Private Placement Initiatives for Local Investors Through Management Buyout and/or Employee Participation Techniques
* Additional Divestiture Techniques: Voucher Schemes, Privatization Auctions, and Public Offerings
* Understanding the Implications of a Government "Golden Share"
* Determining the Level of Foreign Participation in Privatization
* Foreign Investment Case Study: Zambia SOE

iv. Marketing the State-Owned Asset for Privatization: Developing Appropriate Contact Strategies

* Preparing Profile Documents on the Asset: Techniques for Product Positioning
* Identifying Appropriate Buyers for Investment Opportunities: Local and Foreign Focus

* Utilizing the Media for Public Relations/Awareness: Increasing the Number of Prospective Investors
* Mobilizing Appropriate Financial Institutions for Debt and Equity Participation
* Case Study: Nepalese Tea Company

v. Closing the Deal: Implementing Privatization Transactions

* Determining the Terms of the Sale: Understanding the Objectives and Concerns of the Prospective Investors
* Determining the Terms of the Sale: Understanding the Objectives and Concerns of the Government
* Developing Strategic Guidelines for Negotiations: Insurance that Government Interests are Protected
* Importance of Warranties for Transparency Issues
* Case Studies: Bangladesh Textile Industry and a Zambian Milling Company Case

vi. Post-Privatization Monitoring and Evaluation

Although this was the original outline for the two, five-day workshops, in actual implementation, several items were given different emphasis. For example, the team spent time on labor redundancy issues and minority share ownership techniques that were not originally listed on the outline. Additionally, we included a simulated negotiation exercise on the last day of the workshop that was not originally scheduled but which we felt was critical for the learning curve of the participants in attendance.

PARTICIPANT LISTS

ZAMBIA PRIVATISATION AGENCY

Training Seminar

MANCHINCHI BAY LODGE
SIAVONGA

COURSE ONE: MAY 17 - 21, 1993

LIST OF PARTICIPANTS

Zambia Privatisation Agency

	NAME	DEPARTMENT	TITLE
1.	Mr James Matale	Management	Director
		PLANNING & DEVELOPMENT	
2.	Mr Stephen Mwamba		Head
3.	Mr Francis B C Mutale		Sen. Tech. Off.
4.	Ms Lydia Mukuka Malama		Sen. Tech. Off.
		FINANCE, ECONOMIC & BUSINESS	
5.	Mr Jester Njekwa Katanekwa		Sen. Tech. Off.
6.	Mr Charles Muwe Mungule		Sen. Tech. Off.
7.	Ms Chalwa Mukonde Cheelo		Tech. Off.
		SOCIAL IMPACT	
8.	Mr Misheck Zulu		Tech. Off.
9.	Ms Grace Mulemba Njiko		Tech. Off.
		PUBLICITY & MARKETING	
10.	Ms Chipo Mweetwa		Head, Publicity

LINE AGENCIES

Ministry of Commerce, Trade & Industry

11.	Mr Ngosa Chisupa	Economist
12.	Mr Frank Chipimo	Economist

Ministry of Information & Broadcasting

13. Mr Patrick Jabani

<u>Ministry of Labour & Social Security</u>

14. Mr Jim Kalikeka

<u>Ministry of Legal Affairs</u>

15. Ms Elsie Mulundu Mabula — State Advocate

<u>Ministry of Agriculture, Food & Fisheries</u>

16. Ms Lomthunzi Jere — Economist & A/Head, Financial Analysis Section

<u>Ministry of Mines and Mineral Development</u>

17. Mr Phineas Zulu — Economist

<u>ZIMCO Limited</u>

18. Mr Maliwa A Lubasi — Senior Economist

<u>MEDIA</u>

<u>Zambia National Broadcasting Corporation</u>

19. Mr Ben Kangwa — Producer, Business Review

<u>Times of Zambia</u>

20. Ms Ing'utu Muyambango — Snr. Business Reporter

<u>Financial Mail</u>

21. Mr Charles Kakoma — Business Editor

<u>Weekly Post</u>

22. Mr Tendai Banda — Reporter

<u>Zambia News Agency (ZANA)</u>

23. Mr Ken Liayo — Reporter

ZAMBIA PRIVATISATION AGENCY

Training Seminar

MANCHINCHI BAY LODGE
SIAVONGA

COURSE TWO: MAY 24 - 28, 1993

LIST OF PARTICIPANTS

Zambia Privatisation Agency

	NAME	DEPARTMENT	TITLE
1.	Mr Siakatanta Siamuleya	Management	Board Secretary

PLANNING & DEVELOPMENT

2.	Mr Andrew Chipwende	Sen. Tech. Off.
3.	Mr Patrick Bulundo	Tech. Off.
4.	Ms Claire K Limbwambwa	Sen. Tech. Off.

FINANCE, ECONOMIC & BUSINESS

5.	Mr Fabiano Chipasha Lukashi	Head, FEB
6.	Mr Edward M S Singosho	Sen. Tech. Off.
7.	Mr Laston Mulenga Kaluba	Sen. Tech. Off.
8.	Ms Yvonne K Saini	Sen. Tech. Off.
9.	Mr Henry Sakala	Sen. Tech. Off.
10.	Ms Charity N N Chizyuka	Tech. Off.

SOCIAL IMPACT

11.	Ms Elizabeth B Jere	Head, Impact

PUBLICITY & MARKETING

12.	Mr Kenneth Mulena	Sen. Tech. Off.
13.	Ms Judith M Munjoma	Sen. Tech. Off.

LEGAL

14.	Mr Mudford Z Mwandenga	Head, Legal

LINE AGENCIES

Ministry of Commerce, Trade & Industry

15.	Ms Anessie M Banda	Assistant Registrar, Companies

Ministry of Information & Broadcasting

16.	Mr Patrick A Lungu	Assistant Press Officer

Ministry of Tourism

17.	Mr Reuben Zulu	Senior Economist

Bank of Zambia

18.	Mr Likolo Ndalamei	Senior Economist

Ministry of Agriculture, Food & Fisheries

19.	Mr Julius J Shawa	A/Principal Economist

Ministry of Finance

20.	Mr Edwin Nosiku Siyawayawa	Snr Revenue Inspector

Zambia Congress of Trade Unions

21.	Mr James Mazyopa	Director/Int. Affairs & Public Relations

MEDIA

Zambia National Broadcasting Corporation

22.	Mr Chibamba Kanyama	Programme Organiser

Financial Mail

23.	Ms Mary Malama	Business Reporter
24.	Mr Evans Milimo	Senior Reporter

Profit Magazine

25.	Mr David Simpson	Editor

PROGRAM MATERIALS

Day One Materials

The Zambia Privatisation Agency and the Privatization Process

Introduction

The main objective of the Zambia Privatisation Agency (ZPA) is to effectively implement the Zambian privatization program and complete privatization transactions. To do this, however, the roles and responsibilities of the ZPA staff (as well as line ministries and others) must be clearly defined so the privatization process can be completed successfully and in a timely fashion.

As a way to formulate a better understanding of the roles and responsibilities of each individual in the privatization process, we would like to begin the workshop with a short exercise.

Your task on this first afternoon is to complete the following:

1. On a sheet of paper, write down your perceived roles and responsibilities within a) the privatization process in general and b) the ZPA (staff members only).

   You will be allotted 10 minutes to complete this task.

2. We will divide you into groups and each person will have an opportunity to present his/her perceived roles and responsibilities to the group.

   Each group will have 15 minutes to complete this task.

3. After the brief presentations, each group will then create the following:

   > A privatization "flow chart" highlighting the processes of privatization. Built into the flow chart will be an indication (using diagrams) of how you believe the ZPA staff, ZPA departments, ministries, media, etc. should be integrated into this process.
   >
   > Each group will have 30 minutes to complete this task. Each group must turn into the instructors a one-sheet "flow chart" indicating their processes.

The results will NOT be distributed to the general class. This exercise is merely an opportunity for the participants to explore preliminarily the relationships between privatization and ZPA implementation strategies, prior to the actual classwork.

At the conclusion of the workshop, we will conduct a similar exercise where the results will be discussed in a general class session.

USE OF COUNTRY CASE STUDIES

When looking at the experience of other countries, ZPA planners should address the following basic questions, which fall into two categories: six questions designed to analyze the experience of the country being studied; and six which stress self-analysis of their own country's conditions and plans.

Questions to Ponder About the Case Study Country

1. In basic terms, what were they actually trying to do?
2. What were the conditions that prompted them to do this?
3. What were their short-range objectives and strategies?
4. What were their long-range objectives and strategies?
5. What did they accomplish, and how?
6. Where did they fail, and why?

Questions to Ponder About Zambia's Situation and Plans

1. What do we want to accomplish in the long run?
2. What do we want to accomplish in the short run?
3. What is our plan of action?
4. What factors will most affect our efforts, both positively and negatively?
5. What can we adapt from the other country's experience?
6. What must we do differently, and why?

This approach may seem simplistic to some, but it strikes to the core of our purpose. Each factor, each step in the process of privatization, should be scrutinized through the prism of these and similar questions. Such application, done with thoughtfulness, candor, and consistency can transform the comparative case study from a document to be read into a tool to be used. The key to success is the willingness to face difficult issues squarely and to engage in rigorous self-analysis.

When we finish investigating various case studies and have gone through the overall workshop agenda, we should come back to these and similar questions as a reflective exercise during our final evaluation of how the ZPA should proceed as the country goes through its privatization program and accompanying socioeconomic transition.

DETERMINING THE FRAMEWORK FOR SUCCESSFUL PRIVATIZATION IMPLEMENTATION

I. Geographic and Substantive Overview of Privatization

Brief survey of privatization activities worldwide
- types and places

Reasons for building state enterprise systems

Reasons for privatizing

Brief listing of types and methods of privatization

Propositions and caveats for approaching privatization

II. Enabling Environment for Privatization - Opportunities and Constraints

Political considerations

Economic conditions, policies, and programs

Legal and regulatory environment

Public administration, control systems, and the bureaucracy

Social patterns and traditions

III. Design of Privatization Strategies

Long-range goals and short-range objectives of the privatization program - pragmatism vs. ideology

Developing a coherent and comprehensive privatization plan - political will

Integration of policies and programs for privatization, private sector development, and national economic progress

IV. Organization for Privatization

Establishment and organization of a central privatization unit and subsidiary committees

Coordination with other government agencies and programs

Coalitions and the opposition

Bureaucratic systems and reform

Public and private sector roles and relations

Role of the international donor agencies

V. Case Studies (and how to use them)

Comparison of two country approaches

Brief description of selected country privatization programs - successes and failures, and why

The public, the media, and privatization

THE ENABLING ECONOMIC, SOCIAL, AND POLITICAL ENVIRONMENT

1. Political environment - past and present

   a. Government organization and policies

   b. Experience with liberalization

   c. Historical and geopolitical influences

2. Economic environment

Policy issues, including liberalization

Role of the government, bureaucratic culture

Legal/regulatory environment and issues

Domestic factors

- agricultural sector and agribusiness
- industrial sector
- service sector
- infrastructure
- labor issues, labor productivity
- experience with privatization
- public/private sector relations

3. Private sector role, stage of development, management competence, social responsibility attitudes

4. Social environment

   Urban/rural differences

   Poverty, standards of living

   Education

   Public awareness and attitudes

   Intellectual and academic communities

   Attitudes toward business and businessmen

   Cultural environment

7 PROPOSITIONS AND CAVEATS FOR APPROACHING PRIVATIZATION

1. One must recognize the reality that for better or worse privatization is often more influenced by political issues than by strictly economic considerations. This is especially true in the case of volatile labor issues.

2. A government's privatization policy will be ineffective unless it is preceded by a well thought-out strategy with clearly defined long-range objectives, backed up with political will and commitment, and implemented through a well organized unit and a long-term action plan that is coherent, comprehensive, coordinated, and consistent.

3. One should approach this subject from the standpoint of privatization of an <u>economy</u>, not merely the unloading of inefficient, money-losing state enterprises. Privatization should be undertaken to develop viable enterprises and a more vibrant and better balanced economy, not primarily to cut state enterprise losses and reduce government deficits.

4. Conditions that provide a favorable enabling environment and generally promote the benefits of competitive market forces are crucial to the success of private sector development - and privatization and private sector development are <u>inseparable</u>. Privatization of state enterprises will accomplish little without a parallel government-sponsored integrated package of policies and programs that encourages, assists, and cooperates with the private sector. The private sector must be viewed as a partner in national economic development, not as an unsavory competitor.

5. Privatization should be approached as a policy-oriented subject, not a bookkeeping problem. Zeroing in initially on individual state enterprises often obscures this basic point. It also puts the cart before the horse. Analyzing and reforming the policy framework and regulatory environment within which privatization and the private sector must operate is infinitely more productive than rushing to "call in the investment bankers" or "look at the books" of public enterprises that are likely candidates for unloading.

6. Privatization and divestiture are not synonymous. Divestiture is only one type of privatization, and is one of the most complicated, least attractive, and least utilized methods. There are "many roads to privatization," just as there are to its failed counterpart, socialism.

7. Privatization is too often associated primarily with questions of majority equity (especially in the West), but in less developed countries with only embryonic capital markets, partial privatization or privatization of a <u>function</u> or a <u>service</u> can, at times, be very important.

8. The approach to privatization should be pragmatic, rather than ideological, with and emphasis on what is appropriate and feasible in a particular setting - in other words, "what will work in this society, this bureaucracy, and this set of conditions."

9. Transparency, fairness, and integrity must characterize all privatization transactions. Major initiatives should be preceded by sound and objective public education campaigns explaining the program's features and long-term goals. The legitimate concerns of labor must be addressed fairly, along with compensation schemes, retraining and other programs to minimize effects of any unavoidable personnel retrenchment.

10. There is no standard formula for privatization. Conditions, problems, strategies, and solutions will vary from country to country, although most of the more basic privatization and development issues will appear almost everywhere, transcending cultural barriers. Innovators and change agents should empathetically tailor their efforts to local situations, conditions, and patterns, while guarding against the tendency of traditional societies undergoing painful, often traumatic transition to use distinctive circumstances and socio-cultural patterns or traditions as a convenient shield to avoid taking action on needed change.

11. Privatization is a <u>means</u>, not an end. It is not a panacea for curing the ills of a sick economy. Privatization is fraught with political, social, and economic problems, pitfalls and risks. Its implementation is characterized by controversy, nagging uncertainties, and few short-term victories. Half-measures only seem to bring about frustration and unfulfilled objectives and aspirations. Unquestionably, privatization is untidy business.

If all this is true, why would any government leader in his or her right mind opt to follow a course of privatization? They are doing so in increasing numbers for the same reason that people chose democracy and surgical operations - while not completely reassuring or satisfying, they (and privatization) are certainly preferable to the alternative.

In the final analysis, the success or failure of any country's privatization effort will largely depend on a willingness to engage in rigorous self-analysis, to evaluate its program's design and performance against the criteria in the eleven points above, and to face vested interests and sensitive issues squarely with sustained political will as the country goes through its own particular socio-economic transition.

Excerpted from Clare E. Humphrey: <u>Privatization in Bangladesh: Economic Transition in a Poor Country</u> (Boulder, Colorado, Westview Press, 1990).

COMPARISON OF TWO COUNTRY PRIVATIZATION PROGRAMS

Similarities Between the Two Countries

- an agriculture-based economy, featuring small holdings and a high percentage of landless farmers;
- a conservative, traditional society;
- a colonial background, wherein the economy has been geared to the needs of the colonial power;
- a backwater area dominated by nearby major commercial and industrial centers;
- some infrastructure built by the former ruling power;
- a densely populated area, with the majority of the population in rural areas;
- almost no natural resources;
- a large pool of unskilled labor and widespread poverty;
- few indigenous entrepreneurs or managers with top-level experience;
- a business community oriented toward trade and commerce, not industry, and a tradition of familial rather than corporate structures;
- an economy shattered by war;
- 80%+ of industrial capacity residing in the public sector;
- almost no capital markets and limited domestic savings;
- an industrialized sector heavily nationalized after departure of a foreign power; and
- encouraging prospects for considerable foreign aid.

Privatization Strategy and Implementation by Taiwan

- a gradual step-by-step, pragmatic approach to economic development, starting with agriculture, which has driven industry; building up infrastructure and early emphasis on small and medium labor-intensive fields and enterprises;

- careful planning with clearly identified short and long-term objectives, staring with currency stabilization;

- scrupulous attention to organization and details;

- demonstrated political will through consistent support of policies; policy statement followed by actual implementation;

- an integrated set of practical programs promoting private sector activity; smooth and timely transition from import-substitution to export orientation, labor-intensive activity into high tech operations, and evolvement from assembly type operations into manufacturing;

- rationalization of the regulatory and administrative environment;

- promotion of cooperation between the bureaucracy and the business community and efforts to decease friction;

- a privatization policy coordinated with other economic, fiscal, and social policies, including employment issues;

- a planned, structured approach to transition of enterprises from the public sector to the private sector, and conscientious attention to follow-up after privatization;

- privatization transactions and negotiations conducted with fairness and honesty;

- simplified procedures, drastically reduced bureaucratic interference, and curtailment of corrupt practices; and

- effective use of foreign aid.

Day Two Materials

Developing a Country Profile

Three General Areas of Information in the Profile

Business History and Financial Condition

Operations and Management

Marketing and Strategic Position

Profile Should Reflect Information on the Company in Present Condition

Profile Should Also Reflect Anticipated Effects of Privatisation

Elements of Business History and Financial Condition

Macro Economic Data and General Information

Description of the History of the Enterprise and Nature of the Business

Significant Developments or Changes in the Enterprise

Historical Financial Statements (5 Year History)

Summary of Long Term Debt and Payment Schedules

Aged Receivables

Cash Flow

Government Subsidies

Financial Performance of Operating Units

Elements of Operations and Management

Description of Management and Key Personnel

Employment and Staffing Data

Details of Each Business Location

- Functions Performed
- Operational Capacity
- Description of Assets and Their Condition
- Inventory Levels
- Photographs

Working Capital Requirements

Capital Expenditure Requirements

Elements of Marketing and Strategic Position

- Description of the Markets in which the Business Operates
- Company's Position within the Markets
- Dependence on Government Preferences
- Advantages and Disadvantages of the Company
- Intangible Assets
- Strategic Plans

Accounting and Financial Analysis

- The Concept of Stocks and Flows
- Analysis of Financial Statements
  - Balance Sheet
  - Income Statement
  - Ratio Analysis
- Income and Cash Flow
- Compound Interest and Present Value

Valuation Theory

"Value" Must Be Defined

Value is Based upon Expectation of Future Benefits

Value is Dependent on Time and Circumstances

Relationship between Cost and Value

Three Approaches to Value

- Market Sales Comparison Approach
- Cost Approach
- Income Approach

Valuation of Assets

- "Value in Use" or "Value in Exchange"
- Valuation by Depreciated Replacement Cost Method
- Replacement/Reproduction Cost
- Physical Deterioration
- Functional Obsolescence
- Economic Obsolescence

Valuation of a Business Enterprise

The Discounted Cash Flow Method

Developing Pro Forma Financial Statements

Valuation in an Inflationary Environment

Valuation of Equity or All Capital - The Debt Free Model

Establishing an Appropriate Discount Rate

Assessing the Reasonableness and Reliability of the Conclusions

Assumption of Debt by the Buyer

Selling at a Loss

Issues in Valuation of Shares

- Lack of Control
- Marketability

Legal Considerations in Preparing for Privatisation

Rights of Employees, Shareholders, Creditors, Third Parties

Conversion of Legal Form of the Enterprise

Transfer of Assets

Selling Below Book Value

Monopolies and Other Special Arrangements

Financial Restructuring for Privatisation

Write Down of Assets

Disposition of Debt

Transfer of Assets

Other Considerations in Preparation for Privatisation

Change in Staffing

Management Cooperation

Economic Rehabilitation of the Enterprise

PRACTICE PROBLEMS

Compound Interest and Present Value

1) A bank deposit of K50,000 is made today, with a fixed interest rate of 20% per annum. The interest is paid once each year at the end of the year, and all interest is left in the account to earn compound interest.

What will the account balance be at the end of 1 year?

What will the account balance be at the end of 3 years?

What will the account balance be at the end of 10 years?

2) A businessman expects to need K10,000,000 in four years. He has an opportunity to invest in a fixed interest security that pays 32% annual interest. Interest is compounded annually.

How much Money must he invest today so that he will have the needed K10,000,000 in 4 years?

At the end of the 4 year period the businessman needs only half of the K10,000,000. If he leaves the other half in the investment, how much will the investment be worth after an additional 2 years (6 years from today)?

3) Calculate the present value of a future cash amount for the following conditions:

K300,000 to be received in 6 years, discounted at a rate of 35%.

K2,500,000 to be received in 2 years, discounted at 90%.

K65,000 to be received in 8 years, discounted at 6%.

US$500 to be received in 5 years, discounted at 12%.

4) An investor has an opportunity to buy an interest in a short term business opportunity. She believes that the investment will return K15,000,000 in the first year, K25,000,000 in the second year, and K30,000,000 in the third and fourth years. She expects no additional return after four years.

Calculate the amount the investor will pay for this opportunity if she requires a 30% return on her investment.

Calculate the value of the investment using a 40% discount rate.

Discounted Cash Flow Analysis
Africa Machine Products
Assume Permanent Employment Freeze
(K1,000,000's)

	1994	1995	1996	1997	1998
Turnover	----	----	----	----	----
Sales of Goods	11,500	11,960	12,438	12,936	13,453
Contract & Repair Svc.	2,400	2,496	2,596	2,700	2,808
	------	------	------	------	------
Total Turnover	13,900	14,456	15,034	15,636	16,261
Direct Costs					
Wages	4,500	4,500	4,500	4,500	4,500
Materials	1,840	1,914	1,990	2,070	2,153
Equipment Depreciation	2,800	2,950	3,100	3,250	3,400
Other Direct Costs	1,946	2,024	2,105	2,189	2,277
	------	------	------	------	------
Total Direct Costs	11,086	11,387	11,695	12,009	12,329
Gross Profit	2,814	3,069	3,339	3,627	3,932
Operating Expenses					
Administrative Salaries	2,000	2,000	2,000	2,000	2,000
Selling Expenses	1,112	1,156	1,203	1,251	1,301
Other Operating Expenses	1,807	1,879	1,954	2,033	2,114
	------	------	------	------	------
Total Operating Expenses	4,919	5,036	5,157	5,283	5,415
Operating Profit	(2,105)	(1,967)	(1,818)	(1,657)	(1,483)
Income Tax	277	273	271	272	275
	------	------	------	------	------
Net Income	(2,382)	(2,240)	(2,089)	(1,928)	(1,757)
Cash Flow Adjustments					
Depreciation Addback	2,800	2,950	3,100	3,250	3,400
Capital Expenditure	(1,500)	(1,560)	(1,622)	(1,687)	(1,755)
Change in Net Wkg. Capital	0	(39)	(40)	(42)	(44)
	------	------	------	------	------
Total Cash Flow Adj.	1,300	1,351	1,437	1,521	1,601
Net Cash Flow	(1,082)	(889)	(652)	(408)	(156)
Discount Rate	20%				
Present Value Factor	0.833	0.694	0.579	0.482	0.402
Present Value	(902)	(618)	(377)	(197)	(63)
PV of 5 Year Cash Flow	(2,156)				
Terminal Value (3 x C.F.)	(468)				
Present Value Factor	0.402				
P.V.of Residual	(188)		Enterprise Value		(2,344)

Discounted Cash Flow Analysis
Africa Machine Products
Assume 2 Year Employment Freeze
(K1,000,000's)

	1994	1995	1996	1997	1998
Turnover					
Sales of Goods	11,500	11,960	12,438	12,936	13,453
Contract & Repair Svc.	2,400	2,496	2,596	2,700	2,808
Total Turnover	13,900	14,456	15,034	15,636	16,261
Direct Costs					
Wages	4,500	4,500	2,706	2,814	2,927
Materials	1,840	1,914	1,990	2,070	2,153
Equipment Depreciation	2,800	2,950	3,100	3,250	3,400
Other Direct Costs	1,946	2,024	2,105	2,189	2,277
Total Direct Costs	11,086	11,387	9,901	10,323	10,756
Gross Profit	2,814	3,069	5,133	5,312	5,505
Operating Expenses					
Administrative Salaries	2,000	2,000	1,298	1,350	1,404
Selling Expenses	1,112	1,156	1,203	1,251	1,301
Other Operating Expenses	1,807	1,879	1,954	2,033	2,114
Total Operating Expenses	4,919	5,036	4,455	4,633	4,819
Operating Profit	(2,105)	(1,967)	678	679	686
Income Tax	277	273	271	272	275
Net Income	(2,382)	(2,240)	407	407	412
Cash Flow Adjustments					
Depreciation Addback	2,800	2,950	3,100	3,250	3,400
Capital Expenditure	(1,500)	(1,560)	(1,622)	(1,687)	(1,755)
Change in Net Wkg. Capital	0	(39)	(40)	(42)	(44)
Total Cash Flow Adj.	1,300	1,351	1,437	1,521	1,601
Net Cash Flow	(1,082)	(889)	1,844	1,928	2,013
Discount Rate	20%				
Present Value Factor	0.833	0.694	0.579	0.482	0.402
Present Value	(902)	(618)	1,067	930	809
PV of 5 Year Cash Flow	1,287				
Terminal Value (3 x C.F.)	6,040				
Present Value Factor	0.402				
P.V.of Residual	2,427		Enterprise Value		3,714

Discounted Cash Flow Analysis
Africa Machine Products
(K1,000,000's)

	1994	1995	1996	1997	1998
Turnover	----	----	----	----	----
Sales of Goods	11,500	11,960	12,438	12,936	13,453
Contract & Repair Svc.	2,400	2,496	2,596	2,700	2,808
	------	------	------	------	------
Total Turnover	13,900	14,456	15,034	15,636	16,261
Direct Costs					
Wages	2,502	2,602	2,706	2,814	2,927
Materials	1,840	1,914	1,990	2,070	2,153
Equipment Depreciation	2,800	2,950	3,100	3,250	3,400
Other Direct Costs	1,946	2,024	2,105	2,189	2,277
	------	------	------	------	------
Total Direct Costs	9,088	9,490	9,901	10,323	10,756
Gross Profit	4,812	4,966	5,133	5,312	5,505
Operating Expenses					
Administrative Salaries	1,200	1,248	1,298	1,350	1,404
Selling Expenses	1,112	1,156	1,203	1,251	1,301
Other Operating Expenses	1,807	1,879	1,954	2,033	2,114
	------	------	------	------	------
Total Operating Expenses	4,119	4,284	4,455	4,633	4,819
Operating Profit	693	683	678	679	686
Income Tax	277	273	271	272	275
	------	------	------	------	------
Net Income	416	410	407	407	412
Cash Flow Adjustments					
Depreciation Addback	2,800	2,950	3,100	3,250	3,400
Capital Expenditure	(1,500)	(1,560)	(1,622)	(1,687)	(1,755)
Change in Net Wkg. Capital	0	(39)	(40)	(42)	(44)
	------	------	------	------	------
Total Cash Flow Adj.	1,300	1,351	1,437	1,521	1,601
Net Cash Flow	1,716	1,761	1,844	1,928	2,013
Discount Rate	20%				
Present Value Factor	0.833	0.694	0.579	0.482	0.402
Present Value	1,430	1,223	1,067	930	809
PV of 5 Year Cash Flow	5,459				
Terminal Value (3 x C.F.)	6,040				
Present Value Factor	0.402				
P.V.of Residual	2,427		Enterprise Value		7,886

Superior Manufacturing Co.
Income Statement
($1,000's)

	1989	%	1990	%	1991	%
Turnover	13,712	100.0	14,928	100.0	9,807	100.0
Cost of Goods Sold	6,142	44.8	6,703	44.9	5,682	57.9
Gross Income	7,570	55.2	8,225	55.1	4,125	42.1
Administrative Expenses	1,630	11.9	1,790	12.0	1,470	15.0
Selling & Marketing	2,201	16.1	2,321	15.5	2,019	20.6
Depreciation	821	6.0	829	5.6	835	8.5
Interest Expense	410	3.0	460	3.1	490	5.0
Total Operating Expenses	5,062	36.9	5,400	36.2	4,814	49.1
Operating Income	2,508	18.3	2,825	18.9	(689)	-7.0
Income Tax (35%)	878	6.4	989	6.6	0	0.0
Net Income	1,630	11.9	1,836	12.3	(689)	-7.0

Superior Manufacturing Co.
Income Statement
($1,000's)

	1989	1990	1991
Turnover	13,712	14,928	9,807
Cost of Goods Sold	6,142	6,703	5,682
Gross Income	7,570	8,225	4,125
Administrative Expenses	1,630	1,790	1,470
Selling & Marketing	2,201	2,321	2,019
Depreciation	821	829	835
Interest Expense	410	460	490
Total Operating Expenses	5,062	5,400	4,814
Operating Income	2,508	2,825	(689)
Income Tax (35%)	878	989	0
Net Income	1,630	1,836	(689)

Superior Manufacturing Co.
Balance Sheet
($1,000's)

	1989	1990	1991
Current Assets	----	----	----
Cash	1,390	3,574	2,374
Raw Materials	5,208	4,931	5,209
Finished Goods	8,352	8,599	7,476
Debtors	2,107	1,920	5,463
	-----	-----	-----
Total Current Assets	17,057	19,024	20,522
Long Term Assets			
Plant & Equipment	16,459	15,630	14,795
	-----	-----	-----
Total Long Term Assets	16,459	15,630	14,795
Total Assets	33,516	34,654	35,317
Current Liabilities			
Creditors	5,307	5,822	6,404
Short Term Loans	2,200	1,200	2,000
	-----	-----	-----
Total Current Liab.	7,507	7,022	8,404
Long Term Liabilities			
Long Term Bank Loans	1,963	1,750	1,720
	-----	-----	-----
Total Long Term Liab.	1,963	1,750	1,720
Total Liabilities	9,470	8,772	10,124
Owner's Equity			
Paid Capital	20,000	20,000	20,000
Retained Earnings	4,046	5,882	5,193
	-----	-----	-----
Total Equity	24,046	25,882	25,193
Total Liab. & Equity	33,516	34,654	35,317

<u>Philippine Cotton Case</u>

For case discussion the participant should read the Philippine Cotton case in the binder of readings provided for this course. This case will be used for illustration and discussion of profiling a company targeted for privatization, and to consider issues in valuation.

The following issues will be discussed:

1) From the data provided in the case, briefly outline the information that should be included in a company profile. Remember that any information that a buyer or seller of the business or its assets would want to have in making a buy/sell decision is appropriate for inclusion in the profile. Much of the information appropriate for the profile is included in the case description, but some is not. Identify in your outline profile both items which are available from the written case and those items which are not. There is some judgement involved in establishing a company profile, so there is not an absolute correct solution.

2) What does Philippine Cotton have to sell that would interest a buyer? Is the value based upon tangible assets, intangible assets, or a combination of both?

3) How reliable do you think the valuer's projections are for operating turnover at the San Juan and San Fabian gins in the case where both were to be operated?

4) Would a cost approach analysis be appropriate for valuing any of the three gins owned by Philippine Cotton? In a cost approach analysis would there be any functional obsolescence? Any economic obsolescence?

Day Three Materials

PRIVATIZATION TECHNIQUES AND METHODOLOGIES

Divestiture Techniques and Methodologies

1. Direct placement negotiated sale - 100% [to selected buyer(s)]

2. Direct placement negotiated sale - 100% [by open competitive bidding by tenders]

3. Flotation of shares - 100% [including common and preferred stock]
   - public offering of shares
   - private sale of shares

4. Sale of partial interest [including awarding of board of directors memberships]
   - "51-49 plan"
   - "49-51 plan"
   - "60-30-10 plan" and variations used in Sri Lanka
   - other percentage sales
   - MBO and ESOPs
   - Golden Share

5. Break-up or spin-offs

6. Liquidation or close down, and sale of assets

Alternatives Techniques and Methodologies to Divestiture

7. Marginalization or "Quiet Liquidation"

8. Management contracts

   - Flat or fixed fee contracts
   - Fixed fee, plus costs
   - Percentage of profits
   - Incentive arrangements
   - Equity participation
   - Performance contracts
   - Other variations

9. Leasing and franchising

10. Restructuring in preparation for eventual privatization [including balancing, modernization, and rehabilitation (BMR)]

HYPOTHETICAL COUNTRY CASE STUDY EXERCISE

I. BACKGROUND SITUATION

The Minister of Finance, who has been designated by the President to be the country's principal privatization official, calls you on the telephone and says he needs your advice on how to proceed with the privatization of selected governmental activities. You are a senior official of the recently established Privatization Agency responsible for oversee all privatization activities (The Privatization Agency is an office of approximately 25 staff. There are several departments within the agency, including planning, company analysis, valuation, public relations, legal, and labor departments.).

While your heart stops momentarily at the daunting prospects of this important, exciting, and challenging assignment, you are pleased that the time has finally come for action and you have been chosen to help formulate a program (even though realizing that as an inevitable result your neck will be stuck out a mile and fully exposed).

Although there has been a lot of public rhetoric and political posturing from the new government's leaders about the need to revitalize the economy by promoting private sector development and by privatizing several hundred large and small state-owned enterprises (SOEs) and public service organizations, actual transferring of these public entities from the public to the private sector is only now beginning.

Also, you have been disappointed that the government has never really articulated a coherent policy or offered an integrated package of programs that would effectively promote private sector development and a more balanced and vibrant economy. The main motivations seem to have been to dump unprofitable SOEs (many with negative net worth and all with low productivity and bloated, unmotivated staffs) and, thereby, decrease government deficits.

In the meantime, the country's economy continues to deteriorate as the result of falling commodity prices, the continuing foreign debt-servicing burden, rising local debt (including the federal deficit), all of which have reduced the government's capacity to absorb the SOE losses or invest in their capital needs (or even keep up reasonable maintenance). The still small but growing and more vigorous private sector has taken a wait and see attitude.

Your immediate response to the Minister is,"What do you want done and when do you want it?" His response is,"That's what you need to tell me. Both the President and I were impressed when you briefed us about what you learned at the CFED Privatization Seminar, and we hope that you can apply some of this knowledge to help us launch the government's privatization program with something concrete that will demonstrate our political commitment and show everyone how we intend to proceed. We want a winner in this first round; and we want to make the public aware of the nature, goals, and long-term benefits of our privatization program."

After further discussion (during which you are certain that your heart beat and blood pressure reached alarming levels), it was agreed that you would prepare a time-bound Action Plan for presentation to the President, the Task Force, and the cabinet. You are to describe how to privatize two large textile mills, describe the objectives to be achieved, alternative approaches to deal with critical obstacles, and how this will fit in with the overall privatization/economic development strategy to be included in the 13th Five-Year Plan (revised). The Minister hangs up. You gulp, catch your breath, thoroughly alarm your devoted staff by calling for an avalanche of files, get your pencils sharpened, and start to work.

II. PROJECT ASSUMPTIONS

MACRO-ECONOMIC CONSIDERATIONS: Your country has a colonial past, during which the local economy and industry tended to favor the interests of the colonial power. A prolonged post-independence experience with a heavily state-controlled economy did not fulfill expectations. The government has recently announced intentions to shift to a more market-driven economic structure. The economy is deteriorating because export earnings have fallen, the budget deficit is rising, and the SOEs are inefficient, over-staffed, producing low quality goods not designed to meet market demands, not competitive internationally, and losing money. The Government has announced an immediate macro-economic revitalization program, involving policy reform, loan and organizational restructuring, austerity measures, and major privatization actions.

COMMERCIAL CLIMATE: The Government has recently announced is relaxing foreign exchange controls, devaluing the currency 20%, phasing out import-substitution policies to favor export-oriented activities, and is rationalizing tariff regimes and import regulations. While realistic about foreign investment in the short range, the Government favors it over bank or government loans because it brings in technology and access to international markets with hard currency.

PRIVATIZATION FRAMEWORK: At present the privatization program is still in its formative stage, although enabling legislation is on the books. The new, popularly elected government's formal policy has only been announced and the number of actual transactions has been minimal. The informal policy declaration that outlined the program included:

<u>Incremental Versus Wholesale Privatization</u>: The President indicated publicly that he preferred carefully selected targets of opportunity that were small to medium in size (no dinosaurs), relatively non-controversial, and which would allow the Government to demonstrate how a nation-wide program could be organized and managed quickly and effectively. In other words, he does not want to chew off more that the Government and business can swallow at this stage. Most importantly, he wants local business to acquire as many of the public assets as possible so that they will support the longer term, major privatization objectives and programs.

<u>Modalities</u>: The President and the Minister of Finance have expressed a desire for full-scale divestiture of commercially viable SOEs that could be acquired by local interests, with direct foreign investment if needed and possible. They are willing to experiment with employee buy-outs. For SOEs with negative net worth and questionable viability, the Government will be prepared to auction or liquidate. For strategic industries and public service activities, long-term leasing

and/or management or performance contracts with incentive packages built in are the preferred modalities.

Financing: The country has a promising but still underdeveloped capital market and a small stock exchange, which is currently being upgraded with the hope that its would be used for the public sale of SOE shares. The hope is that most of the divestiture actions will be through open bidding private sale or flotation of shares, possibly involving foreign investment in joint ventures for the larger, more complex transactions. The Government is willing to experiment with employee ownerships and is exploring alternative ways to provide restructuring and other financial assistance.

Employment: The labor movement is heavily unionized, strong, highly politicized, and hostile to privatization. The President has promised that privatization will not lead to major retrenchment or loss of jobs. The Government will provide training and reemployment programs if any case where limited retrenchment is absolutely necessary, and has established severance pay and early retirement programs.

III. PROJECT SCENARIO - Privatization in the Textile Industry

You and the Ministerial Task Force have decided that an ideal test case would be privatization in the textile sector, which has been an important industry in your country for several generations. The textile sector was chosen because it is a strategically important industry, has a representative cross-section of opportunities and problems, and a good mix of winners and losers. A success here would have multiplier effects throughout the economy.

Relatively good quality cotton is grown in your country, but does not supply more than one-third of the industry's needs; and climatic and soil conditions and other agro-economic factors are such that a significant increase in cultivation is not feasible and probably unprofitable. Up to the present, governments have tended to set the price of raw cotton with the needs and demands of urban voters in mind, and the unorganized farmers have not received a fair price for their cotton.

There are approximately 80 mechanized textile mills in the country, some fairly large with 35-40,000 spindles and over 2,000 employees. The industry's total spindles are in the neighborhood o. 1.2 million, and there are about 12,000 power looms scattered around the country. For the non-textile experts, we should clarify that there are three types of textile manufacturing in your country: spinning (producing thread for fabrics or various types); weaving (producing fabric or cloth of various types, including knitted material and hosiery); and finishing (which includes dyeing, printing, and finishing).

On the average, spinning mills in the public sector about break even, but some are making money, and some are losing heavily. Almost all public weaving mills are unprofitable, although private ones are making profits, and the enormous private cottage industry handloom sub-sector (200,000 looms) is doing rather well in view of the small and underfinanced nature of most units. About 125,000 rural families depend on the handloom work for all or part of their income.

Small units in specialized fields, such as knitting, hosiery, and dyeing/printing/finishing are doing well when their equipment and methods are modern; and the potential for expansion in this sub-sector is encouraging. Large composite (all-purpose) mills try to do too much and end up doing nothing well.

The "modern" industrial sector of the textile industry is a major employer (75,000 workers), and a major source of revenue in both the domestic and export markets. Most of the export earnings, however, are being made by a booming ready-made garments (RMG) sub-sector in factories that require only limited capital outlay and moderate technology. The RMG sub-sector employs over 150,000 otherwise unemployable women, but pays abysmally low wages. The RMG industry has mushroomed from virtually nothing a decade ago to more than 400 small to medium firms that will sell more than US$350,000,000 in goods this year.

One of the major challenges facing the textile industry is that there is little or no backward linkage from the RMG factories to the textile mills, mainly because of tariff policies and the poor quality and high price of the spun yarn and woven fabrics turned out on hopelessly outdated and poorly maintained machinery operated with old-fashioned methods. This is unacceptable in an industry where the technology is changing with incredible rapidity around the world. Your country's textile industry is steadily losing ground and is increasingly non-competitive. In addition, labor productivity is low and management is not uniformly competent.

Approximately half of the mills are in the public sector, with about 55% of the installed capacity, but only 48% of the operating capacity, and 44% of actual production. Most government mills are losing money, although a few are earning modest profits. A significant number are not viable by any standards, and are only still operating because state enterprises never die; they linger on by subsidy and frequent cash infusion and loans that are seldom paid back to the exchequer.

There are frequent requests for large sums to rehabilitate these inefficient mills from the bureaucracy, which has a stake in their survival; but most independent experts believe that this would be money down the drain. It is considered far cheaper and more productive to start from scratch and build a new mill, or at least purchase completely new machinery. The present public mills are land rich, and some of their better constructed buildings are valuable. It's mainly the machinery that are beyond redemption.

The bureaucracy is inertial, unmotivated, incompetent and frequently venal. The Ministry of Commerce and Industry interferes in the day-to-day operations of the mills, often bypassing the lumbering state "corporation" set up to supervise the public sector mills. Mill managers have virtually no autonomy or authority and, consequently, do not seek accountability or take risks.

The public mills are regarded as production units, grinding out products at a ponderous rate with little or no thought to quality or the demands of the marketplace. Inventories are enormous and not moving. The over-staffed mills are politically attractive employment stations. Public mills tend to produce low quality goods and simple native garments for the lower income groups in the domestic market. The public sector bureaucracy and its mills have virtually no marketing strategy. They just fill orders and require cash on delivery for their goods.

The encouraging thing about the industry is that the more recently constructed private mills with new equipment and modern methods are meeting international standards and making money inefficient local industry that is "fat, dumb, and happy."

The labor force is largely, though not completely, urban-based, and is highly organized and politicized. The union steward is often the most powerful man in a mill. National wage policy has been essentially made by political speech and not through normal face-to-face negotiations between labor and management. Labor problems are greatest in the more politicized government mills, but the private sector is forced to follow what the government does in its mills. Strikes are common, costly and sometimes violent.

Infrastructure, transportation, utilities, and distribution networks in your country are not optimal, but adequate.

Private mills are generally better managed and more profitable than most public mills; but modern management is still not widely practiced. Most of the new industrialists have come from traditional commercial trading, and still hold short range views of business development and quick profits. However, at least a half-dozen mills built in the last four years are first rate and are earning respectable profits.

It is obvious that textiles in your country is a complex and troubled industry. It is also obvious that the banking sector is in need of reform. Many loans have been made on other than strictly business criteria. Also, government pressure to make loans keeps shaky mills operating to avoid social impact problems; but this destroys entrepreneurial inefficient local industry that is "fat, dumb, and happy."

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It is obvious that textiles in your country is a complex and troubled industry. It is also obvious that the banking sector is in need of reform. Many loans have been made on other than strictly business criteria. Also, government pressure to make loans keeps shaky mills operating to avoid social impact problems; but this destroys entrepreneurial initiative and rewards failure. Corruption and bribe solicitation is rampant throughout the system. The overall situation has reached crisis proportions and cannot continue.

It has been decided that you will privatize two public mills: Lightning Textile Mill, a 25,000-spindle spinning operation, and Thunder Mills, a large composite mill.

Lightning makes a 3% gross profit before taxes, depreciation, and interest on a production of 3,600 kilotons of cotton yarn; but the mill ends up in the red because of a heavy debt burden (debt service of 12%). The mill has conscientiously tried to pay off its loans and debts, but has gradually fallen behind. Lightning has a complement of 12 officers, 95 staff and 925 workers. It suffers from most of the labor problems of public mills, but the union is at least tractable and relations are stable. Management is considered adequate, but unimaginative. Eight section heads report directly to the mill manager. Two-thirds of its equipment is 15-20 years old, and a third has been purchased in the last decade. It turns over its inventory about three times per year.

The second is Thunder Mills, an composite mill with 20,000 spindles, 500 looms, and a recently rehabilitated dyeing, printing, and finishing section. It does not even make a gross profit, losing at the rate of 5% annually (even before interest,taxes, and depreciation) on a total production of 2,800 kt of 100% cotton yarn, 16 million meters of fabric, and 4 million meters processed through the finishing operation. 80% of its fabric is made from its own yarn, and 25% of the finishing is from its own fabrics. It tends to buy yarn from other state enterprises, but uses some from private sector; and accepts dyeing and finishing work from all quarters. In a desperate attempt to cut costs, Thunder started buying cheaper raw cotton, but ran into customer complaints about quality.

Thunder's spinning machinery is 20-30 years old and the looms are all over 30, while most of the equipment in the finishing section has been bought and installed in the last 5 years. Overall production was up 7% last year, but sales were static; and wages jumped 22% as management switched to 3 shifts in a frantic attempt to increase production (even though the more it produced, the more it lost). Inventories are piling up in response to production quotas from headquarters and because of a non-aggressive sales effort, although the finishing department is showing sparks of life.

Thunder's work force totals 2,060, with 15 officers, 120 staff, and 940 workers in spinning, 760 in weaving, and 225 in finishing. The labor force is very experienced, but unhappy and vocal. Stoppages are not infrequent. Management is frequently changed; and there have rumors of corruption in the lucrative spare parts section as well in obtaining allocations from the state corporation.

Thunder is very heavily in debt. The mill finally gave up even trying to pay, and the debt service is escalating alarmingly (up 23% in the last 3 years).

Both mills are in urban areas with moderately good infrastructure; but Thunder is in an area with unreliable electrical power, which results in frequent, expensive stoppages. It is important to note again that both mills have hidden assets in very valuable land and buildings. Finally, both mills own and operate modest systems of 10-15 small retail outlets that are generally (but not hugely) profitable; and that might be better run if in the hands of individual independent entrepreneurs.

Task Exercise

Your team is to develop an Action Plan for the privatization of each mill. You may use any privatization technique or approach that you feel is appropriate to the situation. However, you must explain your choices and decisions.

- If you decide to float shares, describe the process step by step.

- If selling through tenders, give some idea of how you evaluated bids and screened potential buyers.

- If financial or organizational restructuring is required, figure out a time-bound plan.

- Any form of debt forgiveness program, debt-equity swaps, etc., must be realistic and fair, not a free ride that penalizes the enterprises that tried to pay off.

Remember that the objective is to establish a viable privately owned and operated enterprise in a stable or healthy textile industry.

Another priority responsibility will be to create backward linkages to the mills from the ready-made garment sub-sector.

Bear in mind the need for a favorable enabling environment, so make recommendations about tariff regimes and other policy and regulatory reforms that will help the privatization campaign to succeed and will be beneficial to the industry as a whole. While concentrating on privatization arrangements for two mills, you are in reality launching a strategy for the entire industry and the economy in general.

Speak of labor, marketing and management issues. Remember that the government wants transparency in its privatization transactions and a public awareness campaign to inform the public of the nature goals and benefits of the program.

Time is of the essence. In order to develop the Action Plan, staff members must apply their individual specialty skills into a working group environment. Only by working as a team will your analysis be completed in a timely manner.

Your team must be prepared to make a presentation of your findings and be able to defend them in a class discussion.

HAPPY PLANNING!

Day Four Materials

LABOR ISSUES

1. Overview

Problems of employment, unemployment, and underemployment in the economy and the society

Political ramifications of labor issues

Determination of wage and benefit policies; the role of the government, role of market forces, dialogue among government, labor, and management

Retrenchment and privatization - immediate, eventual, realities and myths regarding

Retrenchment outlook if SOEs fail; creation of jobs in the private sector

Retrenchment and retraining programs, relocation, Golden Handshake programs, small business start-ups for former employees, advance notice, counseling

Absorption of retrenched employees in other government agencies

Attitudes of labor force to working in public or private sector

Determination of staffing, wages and benefits after privatization

Labor-management relations in the private sector

2. Labor unions, their role, make-up, power, integrity, and political influence; role and quality of union leaders (at national, local, and enterprise levels)

Quantitative and qualitative analysis of the workforce (nationally, by industry, by enterprise, and between skilled and unskilled); relationship between wages/benefits and productivity, and wages/benefits and profitability

Employment terms in privatization transaction agreements

Employee Stock Ownership Programs (ESOP)

Labor codes and the possible need for reform/revision

Society's values and moral issues related to employment and privatization

3. Questions to consider

What are the key labor issues in the country?

Do particular industries have special labor problems?

Are the government's labor policies sound, fair, effective?

Does the Labor Code need reform/revision?

Discuss the state of labor-management relations.

Discuss the strengths/weaknesses of the labor force.

FORMULATION OF EFFECTIVE PUBLIC AWARENESS PROGRAM

The following model reflects 4 - step approach towards effective public awareness program.

STEPS IN DEVELOPING EFFECTIVE
PUBLIC AWARENESS PROGRAM

I Identify the target audience

II. Determine of Communication Objectives.

III. Design the message.

IV. Select the Communication tools.

POSSIBLE SOE MARKETING VEHICLES

PROMOTIONAL VEHICLES	TARGET AUDIENCE(S)
Press Releases (Announce Program, Appointments of Personnel, Offerings, & Completed Transactions) **Meetings:** - Talks by Government Officials at Meetings of Chambers of Commerce and Other Business/Banking Groups - Video Presentations Describing Enterprises Being Privatized **Articles** About Privatization or Enterprises in Newspapers and Periodicals **Mailings** Brief Company "Profiles" to Potential Investors, as well as Banks, Brokers, and other Organizations Which May Know of, or Contain, Potential Investors	LOCAL AND REGIONAL INVESTORS
Direct Mail To Embassies of the Privatizing Country, International Banks, Venture Capital Groups, Known Int'l. Investors, Associations of Overseas Nationals **Videotapes** Shown at Meetings or Receptions Hosted by Embassies in Key Foreign Countries **Special Bulletins** U.S. Foreign Commercial Officer in Each U.S. Embassy has Access to Extensive Network of Newsletters & Bulletins Maintained by U.S. Dept. of Commerce & OPIC. Networks of Potential Investors are Mainained by Regional and Int'l. Development Banks (Listing Attached)	FOREIGN INVESTORS AND OVERSEAS NATIONALS

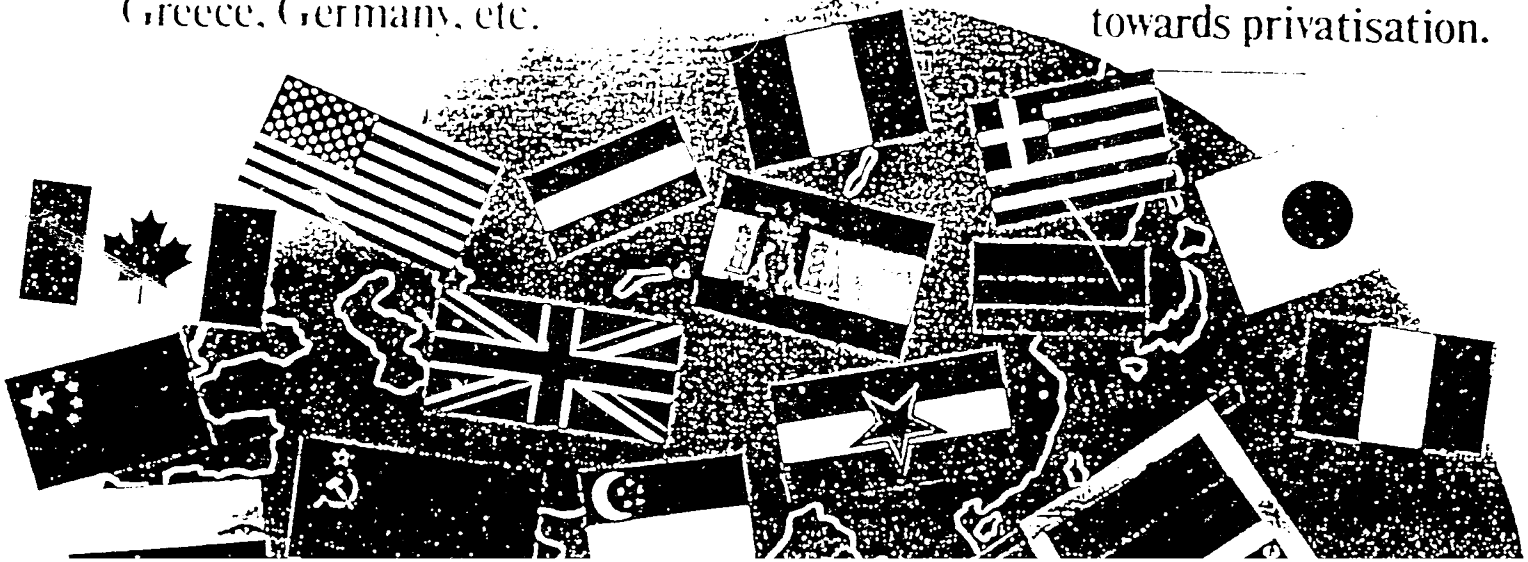
The whole world is going private...

In the Democratic and Socialist World:

Britain, France, Jamaica, Japan, Singapore, Canada, New Zealand, Malaysia, Thailand, Bangladesh, U.S.A., Spain, Italy, Greece, Germany, etc.

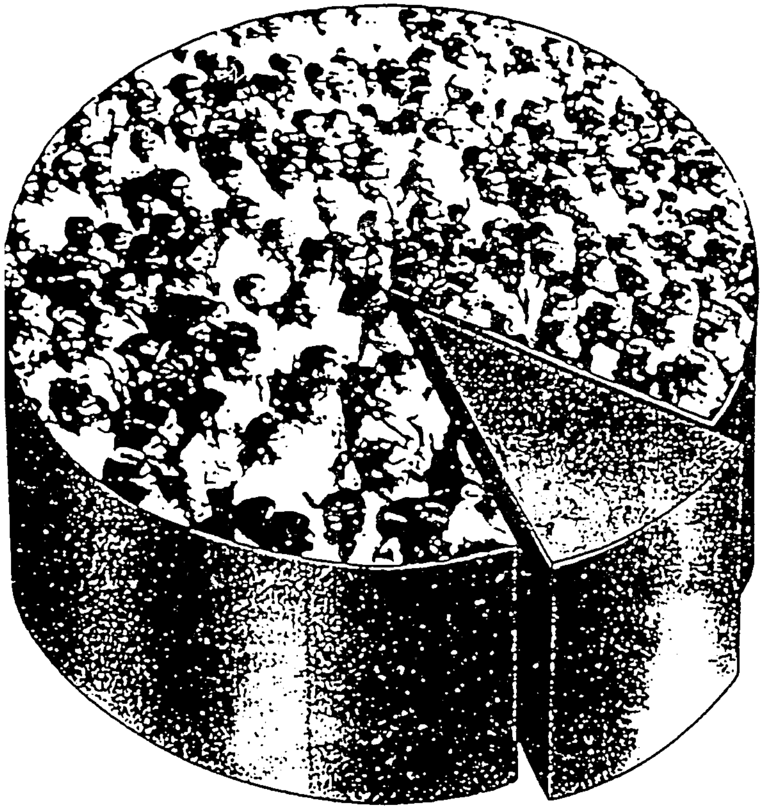
In the Communist World:

China, Hungary, Poland, Yugoslavia, Cuba, U.S.S.R., are also moving towards privatisation.



Have you ever owned a State Corporation?

Privatisation will offer you, a direct major share of the corporate cake!



The need to provide large scale financial assistance to the State Owned Enterprises has drained the national economy and denied the people of the country greater resources for National Development.

In many countries, already, governments have privatised State run business enterprises with impressive success.

As such, should we too not arrest this drain on the national economy by privatising those enterprises of a commercial and business nature, so that they will contribute to the national economy by producing better quality goods and services, providing better terms and conditions of employment, while also offering the people of the country a share in the corporate cake.

From 1984 to 1986 alone, State Corporations have gobbled up Rs. 19,000,000,000 (19,000 million) as subsidies which could have been avoided through proper and accepted management techniques.

This massive sum of money could, for example, have helped double the funds spent on education and health.

The PURPOSE OF PRIVATISATION is to change inefficient State ownership to a profit making, broad-based, share owning Democracy through appropriate management techniques, updated technology, better quality goods and services, better marketing and promotion, effective human motivation, all resulting in increased productivity and profitability.

Will only a few capitalists own and manage such privatised enterprises? NO.

The British experience of privatisation is worthy of emulation, according to which, privatisation contributed to what is nothing less than a transformation of society. For decades, the number of shareholders had fallen as financial institutions came to dominate the share market.

Shareholding was seen as the exclusive province of the rich, which reinforced the conviction that Britain was permanently between "them and us"

Thanks largely to privatisation share issues, the number of shareholders in Britain had almost trebled from three million in 1979 to 8.5 million in 1985... one in five of the adult population.

Privatisation in Sri Lanka will be carried out with the same objective of giving the people of the country and the employee the opportunity to participate directly in the shareholding of privatised enterprises. (Recent share issues have clearly shown that even those belonging to the 2000 - 3000 per month income group, are interested in investing in shares.)

Therefore, for the first time, every citizen of Sri Lanka will be encouraged to buy shares in these privatised enterprises.

Preference will be given to the small investor, and the allotment of shares will be widely dispersed. No single individual will be permitted to buy more than 5% of shares.

The privatised State Enterprises will be professionally managed.

All possible measures will be taken to train existing managers and staff of Privatised State Corporations in accepted management techniques, who will then be motivated by the fact that they are also direct shareholders who will share the profits of their own efforts.

Also you, the public as shareholders will have the direct opportunity of monitoring the progress of privatised enterprises through regular reports, audited accounts and share-holders meetings.

Going Private

For the good of the people!

Why Privatise Profit Making State Corporations?

There are various fears about PRIVATISATION. Especially privatisation of profitable State Corporations. So it is natural to wonder as to why such profit-making ventures should be privatised.

First and foremost, in the context of the investing public, it will not make sense to privatise loss making Corporations. No one will want to invest his or her money in a losing proposition. It naturally follows that the State Enterprises to be privatised must be a viable operation with an untapped potential for further growth, to motivate the investor.

Loss making State Corporations must first be made profitable before being offered for sale to the public.

Furthermore, are profit-making State Enterprises really achieving adequate profits at optimum levels of productivity? Is profitability improving? For profitability to improve, productivity must also increase. With improved productivity even greater profits or lower costs and prices can be achieved and passed to the consumer. Adequate profit on investment is the main objective of Privatisation.

It has been made clear all over the world that the State is not adept at running a business enterprise. Consequently, State owned enterprises provide a poor return on investment.

Controls and procedures inbuilt in the State administrative system make it difficult for a State run business enterprise to achieve high levels of profitability and productivity. The State administrative system seldom promotes the motivation for greater productivity.

Privatisation on the other hand, creates the right environment for efficient management and improved profits through a commitment to agreed corporate goals.

Britain's Chancellor of the Exchequer Nigel Lawson summed up State involvement in business enterprises most effectively with this quote "The business of government is not the government of business."

Lord King, Chairman of British Airways, one of the greatest success stories of privatisation in the UK, has this to say about profitability in State Enterprises:

"The problem with the State sector is that a lot of people do not believe its prime objective is profitability."

Experience in foreign countries show that privatised enterprises have been able to increase profits many-fold.

In the case of Cable & Wireless in UK, since 1981 when it was Privatised, turnover has tripled and profits have increased by 400 per cent.

The lesson of the Jaguar Car Co. turnaround in UK is an outstanding example of what privatisation can achieve. 1980 saw Jaguar make a loss of Sterling Pounds 47.3 million. But by 1985 after privatisation Jaguar turned in a profit of Sterling Pounds 91.5 million and followed that with more than Sterling Pounds 130 million in 1986.

Low profitability continues in State enterprises due to:

1 Lack of motivation of employees. This is due in turn to, absence of effective leadership and proper incentives; redtape; corruption; pilfering; overstaffing and a host of other irregularities. The reasons are mainly peculiar to and inherent in State administrative structure and policies.

2 Low productivity. Mainly due to lack of appropriate management. The resultant low returns on investment and consequent non-availability of funds for updating obsolete machinery and modernising operations contribute to perpetuating a low productivity and low profitability situation.

3 Over-staffing which is caused directly by political pressure to provide employment.

4 Failure of outmoded and restricted marketing, ineffective promotion, poor packaging.

5 Bureaucratic controls and systems which kill initiative, incentive and creativity in management. Insecurity due to shifting political power which adversely affects productivity.

Once privatised the employees themselves will be the shareholders and will demand from Management better returns for their investments and would themselves be motivated towards increased productivity and profitability.

Going Private

For the good of the people!

In just 3 years, State Corporations gobbled up Rs. 19,000,000,000 (19,000 million) that could have been used for greater development and improved welfare services.

C.D.N. July 27, 1988.

82

Why should people always pay the piper... and State Corporations call the tune?

Imagine! Rs 19,000,000,000 (Rs 19,000 million) gone waste! From 1984 to 1986 alone. In just three years. To subsidise State enterprises. That's Rs 19,000,000,000 (Rs 19,000 million), that could have been used, to improve the quality of life in Sri Lanka, better health facilities, better food, better clothing, better shelter, better educational facilities for your children and to produce more jobs; if that Rs 19,000,000,000 (Rs. 19,000 million) could have been channeled into development and welfare.

On the other hand take a quick glimpse at the state of our economy and the unexpected causes that led to the debacle.

In Sri Lanka the damage caused by terrorist activity has necessitated vast expenditure to rehabilitate the economy.

According to the World Bank, the cost to the economy due to the battering taken by terrorism is in the region of Rs. 55 billion. We shall need many more billions to rebuild the economy.

In such strained financial circumstances - including a weighty debt-servicing burden, the Treasury can hardly be expected to continue giving hand-outs to subsidise an ailing State sector.

In the years 1984 to 1986, Treasury expenditure on State Corporations [illegible]

[illegible]

The President on Privatisation

"That is why we decided to have a look into each factory, each state-owned industry or business as an individual enterprise.

For example, we had three or four very useful textile factories - Thulhiriya, Pugoda, Veyangoda and Minneriya. They were running at a loss of Rs. 500 million a year. The Finance Minister had to find that money from the budget.

We called for worldwide tenders and a world famous textile firm entered into a management contract. They are making a profit and producing textiles that are equal to the best textiles in the world.

Looking into not adding to the unemployment problem, not seeking to deprive the worker of his dues, instead of being a burden on the State, we thought of making them public companies. That is the way I look upon privatisation."

President J.R. Jayewardene
on Privatisation
(CDN January 24th, 1987)

Prime Minister of India on Privatisation

"Can we afford a socialism where the Public Sector, instead of generating wealth, is robbing and sucking up the wealth of the poor?"

Rajiv Gandhi
Prime Minister of India
(February 2nd, 1988)

That is why State ventures are being examined for privatisation: to augment government revenue, to promote development in other areas, to promote social welfare and social services, as well as to reduce the burden of taxation on the people. Revenue from Privatisation is an accepted method today of raising revenue for government budgets all over the world.

Revenue from privatisation is itemised as one of the main revenue items in the budgets of several countries. The British Government plans to raise Sterling Pounds 5 billion (nearly 300 billion rupees) every year in the next five years from privatisation for their budget.

France is expecting to raise 35 billion US$ in the next few years from privatisation. Pakistan hopes to raise Rs. 1.8 billion every year for the budget from privatisation in the next few years.

Why increase taxes when you can sell State Enterprises, raise revenue and get rid of managerial problems at the same time. Why should you, the people, needlessly suffer the waste of Rs. 19,000,000,000 (Rs. 19,000 million) spent to subsidise State enterprises? Why shouldn't the country turn the losses into profits and let the people share them?

Going Private
For the good of the people!

CBIKAE

Will privatisation lead to retrenchment, loss of employment and unfair exploitation of labour?

No! And here's why...

In providing the answer to this question we have to examine the present employment situation in State Enterprises

Are State owned Corporations adequately staffed, under-staffed or over-staffed?

It is common knowledge that most State Enterprises are grossly over-staffed which is one of the many reasons for losses that are incurred by many State Enterprises

WILL THERE BE RETRENCHMENT?

Employees of Privatised Enterprises will be assured that there will be no compulsory retrenchment

No employee will be compulsorily retired. However, the option will be offered to any employee who is deemed to be in excess to retire with attractive compensation, if he so desires

Privatisation is an exercise which has its prime objective, increased productivity, through proper management, to achieve adequate profitability. As such, excess staff will be given suitable training and afforded the opportunity to acquire specialised skills so that they could be gainfully employed and contribute effectively towards the effort to achieve new growth and expansion.

The rags-to-riches recovery of the Jaguar Car Company of Britain is a classic case study where privatisation not only brought about increase productivity and increased profits but also created more employment opportunities. Between 1980 and 1984, the period before privatisation, 11,000 workers produced just 14,000 cars per annum – that is, just 1.4 cars per employee. But, by 1985 after privatisation the total jumped to 38,000 cars as many as 3.6 cars per employee with hardly any increase in the number of employees.

In 1980, when Jaguar reached its nadir, the Company made a loss of 47.3 million. But by 1985 the first full year after privatisation, it turned in a profit of Sterling Pounds 91.5 million, and followed that up with more than Sterling Pounds 130 million in 1986.

This increase in productivity and profits through better management, generated more employment opportunities and 3000 new jobs were created. Based on this remarkable turnaround, the projected target now is 80,000 cars a year, by the end of this decade, with profits exceeding Sterling Pounds 300 Million.

Privatisation can lead to similar kinds of results in Sri Lanka – better management, increased productivity and profits and more employment opportunities.

FROM EMPLOYEE TO EMPLOYER AND PART OWNER.

In addition, employees of Privatised State Enterprises will be encouraged to purchase shares through easy payment terms on an instalment basis.

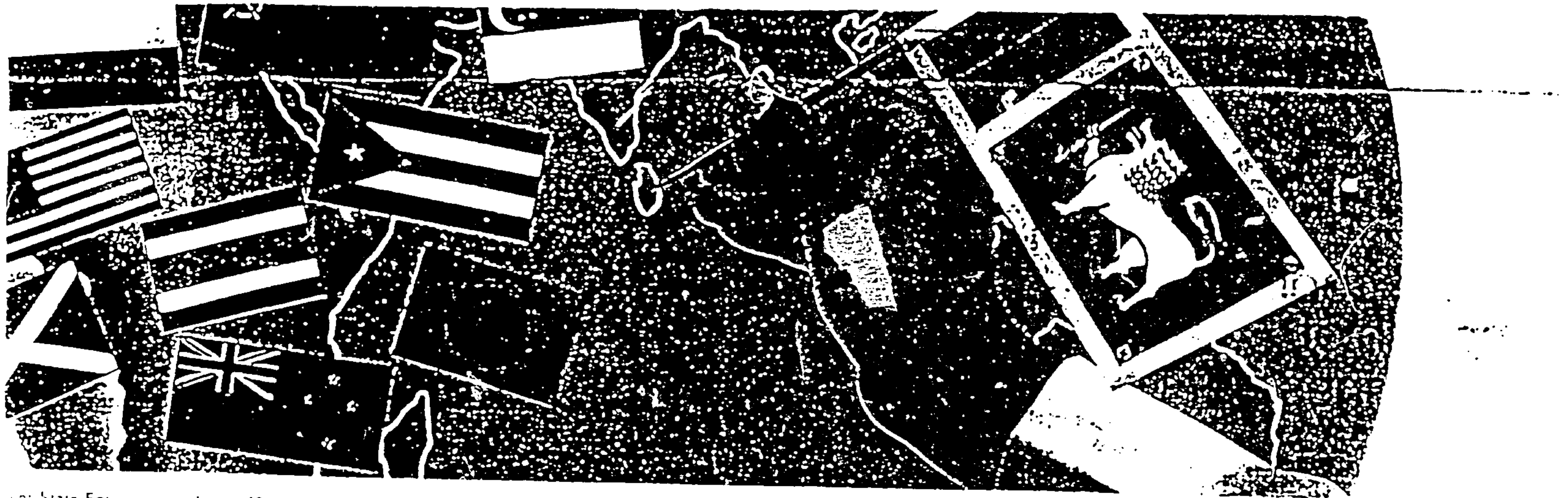
Corporation employees have never had this opportunity before. Privatisation will change that. Their remuneration will change, from salary only to salary and dividends.

With increased productivity and profitability, it should be possible for the employees of these privatised institutions to obtain better terms and conditions of employment. As such, share owning employees of privatised institutions have a better chance of obtaining a better deal than what any State Enterprise could hope to offer its employees.

When the employees have a stake in the enterprise they work for, they will also perform better

This is the philosophy and plan for PRIVATISATION in Sri Lanka Real and direct ownership of the business by the employees and the people in a shareholding democracy

Going Private
For the good of the people!



... State Enterprises something peculiar to ...ka. All over the world, ...emocratic as well as ...munist countries ...tate Enterprises have ... losses and proved a ...drain on Government. The resulting adverse ... the national ... prompted ...ents to seek a viable ... is generally ... that the State ...ation of Commercial ...es does not suit ... commercial ... (Management) ...State Enterprises lack ... commitment ...corporate objectives ...equently have no ...ent towards making ... profits.

... all over the world ...ion of State ...es has transformed ... viable profit making ...

...sation was treated ...icion and hostility ...was first introduced in ...Britain. Now it is an ...part of the economic ... developed and ...ng countries all over ... The speed and ... this global transfor... been breathtaking

over 50 countries have adopted some form of privatisation.

GLOBAL EXPERIENCE

Britain has privatised 20 major State Enterprises and listed several more for privatisation. France has listed 165 for privatisation. Germany, Japan, USA, Canada, Holland, Denmark, Spain and Turkey have done likewise. The Aquino government in the Philippines has recently listed 175 institutions for privatisation, Mexico 236 and Brazil over 100. There are over 165 State ventures privatised already in Latin America and South America, 250 in Asian countries and 30 in African countries. Bangladesh has sold most of its Jute, Textiles, Chemicals and Engineering Industries. Pakistan has privatised rice, cotton and flour mills. Japan has placed its deficit plagued national railways which lost US$ 9.6 billion in 1985 in private hands. Malaysia, Singapore and Thailand and many other African and Asian countries have done likewise. Privatisation has been accepted as a quick, safe and effective way out of a bad economic situation.

In some countries, even public utilities such as railways, ports, bridges, highways, dams, hospitals, gas, water, electricity, ambulances and fire-fighting services, airlines, telecommunications have been privatised with great success, improving profitability through appropriate business management, updated technology, realistic motivation of people and enhanced productivity.

Within the communist framework, China, Hungary, Poland, Yugoslavia and now even Cuba, and the Soviet Union are making positive moves toward privatisation of house ownership, restaurants, shops, small industries etc., which were even unthinkable ten years ago.

In Cuba, the sale of State houses to their tenants, like in Britain, has been a huge success. In China 6,000 flats have passed into private ownership in Shanghai alone, in 1985.

"THE BUSINESS OF GOVERNMENT IS NOT THE GOVERNMENT OF BUSINESS"

BRITAIN'S CHANCELLOR OF THE EXCHEQUER, NIGEL LAWSON

WHAT PRIVATISATION CAN ACHIEVE FOR US

Privatisation has proved to be an effective method of:-

- Improvement in Management efficiency and productivity
- Improving the quality of goods produced.
- Preventing financial drain on the economy
- Augmenting government revenues and releasing greater funds for promoting development, social welfare and social services.
- Help create a new share owning democracy
- Increase national revenue and help reduce turnover taxes

WHY PRIVATISATION?

All over the world repeated attempts have been made to improve the performance of loss making nationalised industries. Few had really got to the root of the problem. It was not that the people working in the industries had lacked talent or dedication. But they were in an impossible position expected to perform as viable businesses but facing interference in their decisions, controls and delays from factors inherent in State sector management. That is why we must Privatise.

PRIVATISATION IN SRI LANKA

In the strained financial and economic circumstances now prevailing in Sri Lanka — including a weighty debt-servicing burden — the State can hardly be expected to continue giving hand-outs to subsidise an ailing State enterprise.

According to President Junius Jayewardene, the architect of Sri Lanka's liberalised economy, "plans for privatisation are not part of an ideology and are not a threat to socialist or communist states or to the socialism that exists in our country. It is purely a question of survival. What is best for our people, not for ever, but for today's circumstances, environment and resources". (Asian Review — March 1988).

Privatisation will be implemented selectively on a case by case evaluation and phased out over a period of time. As such, State sector enterprises will continue to co-exist with privatised enterprises.

Privatisation in Sri Lanka will be carried out with the objective of giving all the people of the country and the employee the opportunity to participate directly in the shareholding of privatised enterprises thereby bringing about for the first time in Sri Lanka a truly broad-based share owning democracy.

Now in Sri Lanka we are on the threshold of privatisation of selected State Corporations. Now for the first time, you, the members of the public, as direct shareholders, will own and earn profits from well managed Privatised Corporations.

GRUKBE

Going Private

For the good of the

Within weeks of assuming office less than a year ago, the Government of Prime Minister Nawaz Sharif announced and began implementing a radical package of economic reforms that remain without precedent in the Third World.

PAKISTAN

vestment in the country. In effect, all monies held in foreign exchange accounts in Pakistan are now fully protected with immunity provided to account holders against any inquiry from the income-tax authorities or any other tax-gathering agency. All balances

CREATES ATTRACTIVE INVESTMENT OPPORTUNITIES

An Economy That Moves With The Times

- Large-scale industrialization
- Privatization of public services and state-owned industry
- Abolition of foreign exchange controls
- Tax and tariff concessions
- Elimination of procedural delays and red tape

Swiftly and decisively, Prime Minister Nawaz Sharif has pulled down awkward government controls and regulations that had inhibited economic growth.

The new government's diagnosis of what ailed the economy was simple and accurate. There were far too may rules, too much red tape, excessive bureaucratic interference. Even the smallest foreign exchange transactions were severely regulated. The formalities for setting up an industrial unit were so numerous that most entrepreneurs gave up half way through the exercise.

All this has now changed. Forever.

"I am proud of the economic changes. We are

held abroad is coming back to Pakistan."

"The government is there to formulate policies. It is not its job to run industry, commerce or hotels."

Prime Minister Nawaz Sharif

Words Backed By Performance

Decisions, no matter how innovative, cannot by themselves persuade investors who need to be convinced if a government's words are backed by performance on the ground.

The government of Pakistan has moved with great speed and on many fronts to demonstrate that it means business.

A high-powered Privatization Commission was set up by the government soon after taking office to dispose of a range of state-owned enterprises, from banks and insurance companies to fertilizer plants, automobile and farm machinery units, engineering works, cement plants, chemical factories, edible oil manufacturing facilities, hotels

percent in imports.

If you are investing in Pakistan, you are on to a good thing. Stay with it.

Big Money Coming To Pakistan

and cost around $ 1.5 billion. Groundwork for the mammoth scheme is scheduled to start later this year.

As the effort to attract investors from around the globe continues, the State Petroleum Corporation along with the Crescent Petroleum Company of

Pakistan opens a window on the Gulf, China, the Soviet Central Asian republics and Iran. It is also playing an important role in the economic reconstruction of Kuwait following the end of the Gulf conflict. Its close and historic ties with China should have a special significance for all investors in the region. The Soviet and Chinese interest in trade and technology exchanges is growing apace and Pakistan hopes to be part of this effort.

"Third World leaders are still capable of reforming and reviving their economies. Pakistan, for example, has recognized that the best prescription for progress is a market economy where government lets men and money loose."

"As a veteran businessman, Sharif knows that you cannot become a capitalist merely by baptism. For countries to successfully

a competitive advantage in terms of local costs. Real estate is much cheaper here and indigenous technical expertise is available at every level."

Multinational global giants such as Toyota, the Imperial Chemical Industries (ICI) and Procter & Gamble have already positioned themselves to take advantage of the attractive opportunities Pakistan offers. This South Asian country enjoys a rich investment climate, generous water resources, excellent agro-processing facilities, ample and fertile farmlands, and a dedicated workforce of 32 million men and women.

Major Investment Conference

In co-ordination with the Multilateral Investment Guarantee Agency (MIGA), a subsidiary of the World Bank, the Government of Pakistan has organized a major international gathering of foreign investors and financiers and their Pakistani counterparts in Islamabad from 18 to 20 November 1991. The message of the Nawaz Sharif government is simple and direct: We are open for business. Come and work with us. Invest in Pakistan.

Enhanced Export Effort

Today, in order to thrive, a country must boost its exports by developing existing markets and discovering new ones. Pakistan is

are also to enjoy exemption from the levy of taxes and otherwise obligatory deductions.

While handing over control of the Allied bank - the second one to be denationalized and put into private hands - to its employees, Prime Minister Nawaz Sharif said in Karachi on 12 August 1991, "I do not believe in slogans but in doing concrete work. The government will provide legal cover to all denationalized units so that in future no government will be able to undo the decision."

Open Door Policy

The open door investment policy initiated and implemented by the government has been extended to include hitherto "no no" areas such as power, transportation and communications. Already, the Paris-based Aga Khan Fund for Economic Development has been given a licence to operate an airline in the private sector to compete with the national carrier, the Pakistan International Airlines (PIA). Ten private groups have been permitted to open banks, which takes the number of such banks in the country to 12. In another bold move, 22 private shipping companies have

". . . we are moving towards making Pakistan an open market."

Prime Minister Nawaz Sharif

Unmatched Industrial and Banking Concessions

In Pakistan today you can:

— set up an industry wherever you like and enjoy tax holidays of up to eight years, along with a host of concessions possibly unmatched in range and scope anywhere in the developing world;

— own 100 percent equity in any venture or purchase shares in an industry on a repatriable basis;

Also:

— repatriation abroad of dividends and other proceeds does not need the Central Bank's clearance;

— there is absolutely no restriction on opening foreign exchange accounts or operating them outside the country. This applies to individuals, companies and investment banks, both local and foreign;

— foreign loans can be arranged by investors without government approval;

— additionally, foreign currency deposits in Pakistan carry an interest rate which is 3/8 percent higher than its European counterpart;

— unspent deposits in local currency, if originally converted from money brought in from abroad, can be reconverted into the desired foreign currency;

— US dollar-denominated bearer certificates can be obtained with a rate of return a quarter percent higher than the relevant LIBOR.

S. Ali Raza, Vice President and Country Manager of the Bank of America in Pakistan, says: "The wide ranging reform introduced in the banking sector, especially with regard to foreign exchange controls, ... a bold step in the right direction. A future government could only undo these decisions at its peril. The clock cannot be turned back. Money

work.

With these radical economic measures in effect, Pakistan is on the threshold of becoming a vital force in the Asian marketplace.

Investing In Pakistan Is Investing In The Future

The figures speak for themselves. Pakistan's gross domestic product (GDP) rose by 5.6 percent in 1990-91, a substantial increase over the average rate of 4.7 percent in the last two years. This dramatic growth was supported by an increase of 5.1 percent in agricultural value added. The large-scale manufacturing sector improved by 4.7 percent while the commodity and service sectors grew by 5.6 and 5.5 percent respectively. The performance of the external sector was even more satisfying, as exports went up by a whopping 24 percent against an increase of 9.6

markets work."

"Prime Minister Sharif understands that in Third World societies government must play a role in establishing an environment that promotes rapid economic growth. That is why he has so firmly committed his fledgling government to wholesale privatization and deregulation, and the scrapping of foreign exchange controls."

Pranay Gupte, Newsweek, July 15, 1991

The international financial community has responded positively to Pakistan's economic reform program. Japan has already established a strong presence in the automobile industry and is now taking a close look at the engineering sector. Major investors in Europe, North America and Asia have also indicated a strong degree of interest in doing business in Pakistan. Joint agreements are being finalized. To name a few, local investors have become partners with the World Bank and Japanese financial houses in the giant Hub River Project, the country's largest power plant which will have a generating capacity of 1,292 MW

Dubai and others, is spending $300 million to $400 million on a hydrocracker project.

At the same time, the Export Import bank of the United States has offered to take part in a joint venture with local private investors in gas-fired power generation plants in Nandipur and Uch. Agreement in principle has been reached with the famous Daewoo Group of South Korea for its participation in a number of enterprises, including the construction of the 315-km Islamabad-Lahore highway.

Listing the many advantages that Pakistan offers, T.Z. Farooqi, Secretary of the Federal Industries Ministry says, "Pakistan offers

has declared 1991-92 as Export Year. In its bold move toward self-reliance and prosperity, a number of steps have been taken. New measures have been added to the incentive package for exporters in the national trade policy announced recently, with foreign companies given permission to enter into the export trade. In 1990-91, the country's exports netted $6.1 billion compared with $4.9 billion a year earlier, an impressive increase of 24 percent. For 1991-92, the target for export receipts is $7.2 billion, an achievable increase of 20 percent over the earlier year.

Permanent Not Ad Hoc Reforms

The Nawaz Sharif government has taken steps to give permanent legal cover to the economic reforms introduced since November 1990. A new law grants protection to reforms pertaining to foreign exchange accounts, banking and foreign and local in-

petition with the state-run Pakistan National Shipping Corporation. Privatization of communications has already started the process of bringing Pakistan on a par with developed countries. Nineteen payphone card operating firms have been granted licences to start services. The state-owned phone and telecommunications sector valued at $5 billion is to be privatized and is up for sale. "The backlog of more than 750,000 applications for phone connections must be cleared by the end of 1992," says Salman Farooqi, Secretary of the Federal Communications Ministry. Meanwhile, contracts for the installation of up to half a million telephone sets have been awarded on a turn-key basis to a group of international companies, including Alcatel, Siemens and NEC.

The message is clear. Here is a country with a vast, largely unexploited investment potential, accompanied by tremendous opportunities for growth and profit. Pakistan is determined that its bid for an economic breakthrough will become one of the great success stories of the last decade of this century.

Pakistan Attracting US Investment

Outgoing US Ambassador to Pakistan Robert Oakley said in Islamabad on 17 August that a number of American companies had expressed keen interest in working in Pakistan as a result of the newly-introduced liberal economic and financial policies of the Nawaz Sharif government. Oakley was of the view that these policies, which he described as "positive", had strengthened the current international trend toward investing in Pakistan.

For further information on foreign exchange reforms and investment opportunities in Pakistan, please contact:
Deputy Secretary,
Ministry of Industries, Block A, Pakistan Secretariat, Islamabad, Pakistan.
Telex: 5774 MIND PK Fax: (92 51) 825130
Tel: (92 51) 823214

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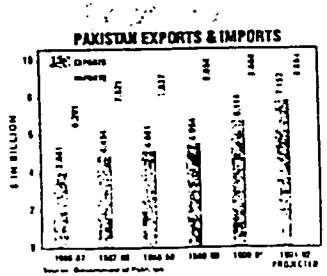

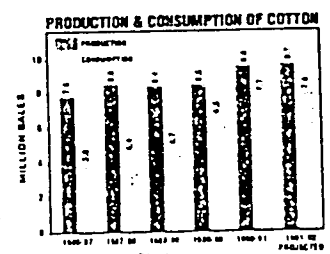

Major Economic Indicators: Pakistan

Average Annual Rates of Increase (1980-89)

	GDP	Industry	Inflation	Exports	Imports
Pakistan	6.4%	7.3%	6.7%	8.5%	4.2%
Low and Middle Income Developing Countries	3.8%	4.5%	53.7%	5.4%	1.4%
OECD Countries	3.0%	2.2%	4.3%	4.1%	5.1%

Source: World Bank, World Development Report 1991

	1991	1992*
Merchandise Exports $ Billion	6.1	7.2
% Increase	23.0	20.0
Merchandise Imports $ Billion	8.7	8.9
% Increase	9.6	2.5
Current Account Balance $ Billion	1.8	0.8
% GDP	4.0	1.5

Source: Government of Pakistan

*Projected

Q&A

QUESTIONS & ANSWERS

1. **Q** **WHAT IS TELECOMMUNICATIONS OF JAMAICA LIMITED?**

A Telecommunications of Jamaica Limited (commonly called TOJ) is the company which owns Jamaica Telephone Company Limited and Jamaica International Telecommunications Ltd. It also owns nearly one-third of Jamaica Digiport International Limited. The first two companies provide all telephone, telex and telecommunications for Jamaica. The Digiport provides specialised private services and is located in Montego Bay.

TELECOMMUNICATIONS OF JAMAICA LIMITED

SHARE INFORMATION

2. Q WHAT IS A SHARE?

A In layman's terms, a share is a part of a company. When you own shares you are part-owner of a company. Owning shares means you can speak and vote at company meetings. You can vote for who you want on the Board of Directors and the company must send you a report every year that tells you how it performed. If the company makes a loss, you do not have to make further payment to the company, even though you are a part-owner.

3. Q WHAT IS THE TELECOMMUNICATIONS OF JAMAICA SHARE OFFER?

A In September the Government is selling some of its shares in TOJ so that more than half of TOJ will be owned privately. Government wants as many people who wish, to have this opportunity. Right now Cable & Wireless and about 3,500 other people together already own nearly half of the Company and Government owns the rest.

4. Q CAN ANYONE BUY SHARES?

A Yes. Anyone can buy shares. No matter what kind of work you do or where you live in Jamaica.

5. Q HOW DO I APPLY FOR SHARES IN TELECOMMUNICATIONS OF JAMAICA?

A You can apply by filling out the application form in the Prospectus. You can use only that form and it must be an original form — not a photocopy.

6. Q WHAT IS THE PROSPECTUS?

A A Prospectus is a booklet that tells you all about a company whose shares are being sold. It also tells you exactly how to buy shares. You should read it before deciding whether to apply for shares.

7. Q WHERE CAN I GET THE PROSPECTUS FOR THE TELECOMMUNICATIONS OF JAMAICA SHARE OFFER?

A In September, the Prospectus will be in the Gleaner and the Record newspapers. You can also get one at commercial banks or at any of the stockbrokers listed at the end of this booklet.

8. Q HOW MUCH TIME DO I HAVE?

A There will be about four weeks from the date of the Prospectus to the time that the applications list will be closed. The list will close at the end of September 1988.

9. Q WHERE WOULD I TAKE MY COMPLETED APPLICATION FORM?

A You would take the form along with your payment to a bank branch near where you live, or to a stockbroker. They can also explain things in the Prospectus and help you fill in the form.

10. Q HOW MUCH WOULD MY SHARE COST?

A You can apply for as little as 200 shares which will cost about $200. You can apply for as many shares as you want but it may be necessary to cut down the bigger applications if people want more shares than are in the offer.

11. Q HOW WOULD I PAY IF I WANT TO APPLY?

A When you apply you would give the bank teller either cash or a cheque. The cheque should be made out to "Duke Corporation" who is handling the applications for the Government.

12. Q WILL I GET ALL THE SHARES I APPLY FOR?

A Government will try to make sure that as many people as possible get the number of shares they apply for and that all applicants get some shares. After the share applications are added up, an announcement will appear in the newspapers to say how the shares are to be divided.

13. Q WHAT IF I DON'T GET THE NUMBER OF SHARES I APPLY FOR?

A The balance of your money will be refunded by cheque which will be sent to you along with the shares which you are allocated.

14. Q HOW WILL I BE ABLE TO PROVE THAT I OWN SHARES?

A You will get a stock certificate, which is a paper that tells how many shares you own. You must always keep your stock certificate in a safe place because you will need it as proof if you ever want to sell your shares.

15. Q IF I DECIDE TO SELL MY SHARES LATER ON, HOW WOULD I DO THAT?

A You would contact a stockbroker who will help you sell your shares or even buy more. All you have to do is call or write to one of the stockbrokers listed at the end of this booklet.

16. Q WHO IS A STOCKBROKER?

A A stockbroker is a person who helps people buy and sell shares. The stockbroker works through the Jamaica Stock Exchange, which is the market where stocks and shares are traded. There is a list of stockbrokers at the end of this booklet.

17. Q WILL MY SHARES ALWAYS BE WORTH THE SAME PRICE I PAY FOR THEM?

A No, not necessarily. The price of shares goes up and down. You can find out how much your shares are worth by reading the Gleaner or the Record. They carry a list of all stocks and the price they are selling for.

18. Q HOW CAN I BENEFIT FROM OWNING SHARES?

A Owning shares is just one way to invest money. Some people invest in a savings account. They put their money in a bank and earn interest on it. Owning shares is not like putting money in a bank account, because the value of shares can go up or down. There are two main benefits that can come from investing in shares: dividends, and more value if the price goes up.

19. Q WHAT IS A DIVIDEND?

A Companies pay their shareholders money called dividends if they make profits and if they do not need to hold the profits in the company. Companies often keep back profits so that the business can get bigger and so the shares can have more value. Most often, companies keep some profits for growth and pay the rest to shareholders. Companies normally pay dividends at least once a year

20. **Q WHAT ARE THE PROSPECTS FOR TELECOMMUNICATIONS OF JAMAICA?**

A Last year Telecommunications of Jamaica made a profit of $198 million. It is the only company licenced by government to provide the general public with telecommunications locally and between Jamaica and the rest of the world. Telecommunications services include telephone, telex and telegraph, among other things. They have this licence for 25 years. TOJ owns Jamaica International Telecommunications (JAMINTEL) and Jamaica Telephone Company. Both of these companies have been profitable over the years and they both provide services (most importantly telephones) that are expected to grow. The prospectus will give full details of the financial status of the company

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OPTIONS FOR PRIVATIZING THE NEPAL TEA DEVELOPMENT CORP.

CASE STUDY ANALYSIS

A Consultant's Report from the Asian Development Bank
to the Ministry of Agriculture
of His Majesty's Government of Nepal

Brief Background on Nepal's Tea Industry

Although tea has been grown in Nepal since 1863, there was no extensive development until 1966, when His Majesty's Government (HMG) established the Nepal Tea Development Corporation (NTDC) as a completely state-owned and operated enterprise. The decision to increase tea production and market it was primarily prompted by increased domestic consumption, although there were some hopes for an expansion of tea exports to Europe and, eventually, America.

By late 1987, the NTDC is running six tea estates. Two are original estates, Ilam and Soktim (which had been operated under private auspices for more than one hundred years) and four other estates or "gardens" have been developed over the years - Kanyam, Tokla, Burnie, and Chillinkot, the last named primarily a research station that has not as yet produced a cash crop. NTDC estates have 2,205 acres under cultivation, comprised of 1,560 acres of mature, producing tea and 645 acres of immature bushes.

Private estates also began developing in the 1960s, prompted by increasing demand and liberalized regulations governing private holdings as a result of land reform. There are presently seven large private estate companies, and an increasing number of small holdings (called "outgrowers"), with a total of 2,011 acres.

Current local production of 1.1 million kg/annum does not begin to meet the estimated domestic demand of 8.8 kg, necessitating enormous imports, mainly from neighboring India, where, paradoxically, cost of tea production is much higher than in Nepal.

Consequently, Nepal's tea industry has an unparalleled opportunity and a challenge to:

- increase acreage under cultivation, including replanting schemes;
- increase yields per acre;
- decrease the necessity for massive imports;
- expand the outgrowers' scheme;
- improve quality standards in growing and manufacture;
- develop more sophisticated marketing practices;
- expand into lucrative international markets, in addition to fulfilling domestic needs;

- improve research and information services and achieve better coordination in the presently fragmented tea industry.

Current Condition of NTDC (in late 1987)

Due to multiplicity of causes - including poor management, overstaffing, corruption, cumbersome bureaucratic systems and procedures, neglect, lack of motivation, poor maintenance, lack of business acumen, and inadequate marketing systems - NTDC has reached a point of insolvency. Long-term debt has accumulated to 58 million rupees (US$1.6 million) and short-term debt totals 6 million rupees ($162,000). Production costs have doubled in the last 4 years, while NTDC's selling price has remained relatively steady (and below private sector levels). Meeting payroll has become increasingly difficult, even intermittent; and maintenance of fields and equipment has deteriorated to a point where performance continues to worsen. Yields and quality are below what they should be. Conversely, all seven private estates are operating profitably, and most are making plans for modernization and expansion.

New board leadership has trimmed about 170 lower clerical staff from a bloated overall roster of 500 (plus field workers), and has instituted other belt-tightening measures. But the Ministry of Finance has provided only 1.5 million rupees out of a budget request of 10 million. British aid, a principal supporter for a decade, has cut off funds because of poor performance, management and government reluctance to institute badly need reforms, and because of the bleak outlook for any improvement.

To analyze and try to resolve some of the problems plaguing the NTDC, the Asian Development Bank (ADB) sent 2 consultants to work with an inter-ministerial team for 2 months. The joint team visited all 6 NTDC estates, plus the firm's headquarters and marketing centers, plus meeting with various officials from the agriculture, industry, and commerce ministries, as well as financial institutions and international donor agencies. Influential representatives of the private sector were contacted, including several private tea companies, among them companies expressing an interest in acquiring NTDC operations and properties.

Some of the important facts and conditions that showed up during the working team's investigations included:

- the estates are all on Royal land, meaning that unless existing laws are changed, the land cannot be sold, only leased;
- there appears to be some price fixing at the small national tea auction, a system that is not working to the advantage of the NTDC as a whole, although some officials might be benefiting personally;
- three of the six estates are in the rich agricultural flat lands known as the Terai, while three are in the

mountains, including the famous garden at Ilam, which is the highest tea garden in the world;
- transportation is difficult in all of Nepal, but especially difficult in the mountains; tea from Ilam and Soktim cannot be brought out by truck, but only by Himalayan pony pack trains;
- while wishing to consider all legitimate bidders and buyers, there is some concern that these valuable tea estates might come under the control of interests from the neighboring giant, India, which dominates so much of Nepal's struggling, subsistence economy; cheap Indian labor is also a concern;
- indigenous capital is greater than many analysts realize, but is still not well developed in the industrial sector; the business community is more accustomed to commercial activity rather than industry; and the tradition is for familial rather than corporate structures; a small stock exchange has only recently been established; Nepal's economy is still very underdeveloped, and poverty and unemployment are widespread;
- five of the estates mainly grow and process the strong powered tea preferred by south Asians, only Ilam produces orthodox leaf tea in the Chinese way;
- four of the estates have tea "factories" or processing plants; the other two ship their tea to the nearest public estate plant; the factories also accept tea for processing from outgrowers and a bit from larger private gardens; the equipment in all four plants is poorly maintained, and is even disappearing in some cases;
- one estate in the Terai (Burnie) has a well equipped, but very under utilized repair shop.

Recommendations and Options for Disposing of NTDC Operations and Properties

The underlying thrust of the recommendations/options is that all commercial operations and functions of the NTDC should be turned over as quickly as possible to the private sector by means of one or more privatization techniques. The revised role of the government would be to establish an underlying policy and regulatory framework conducive to developing a healthy market-driven tea industry, and to providing promotional support, marketing information, and research and extension services.

These revised and reduced government services would be carried out through a newly established Nepal Tea Board, an official body which would provide the support services mentioned above, but which would not operate in the way normally associated with agricultural sector commodity boards. In other words, the government should promote and monitor the industry, but the private sector will run it, and the market will determine prices. The advisory team wanted it firmly kept in mind that the purpose of the exercise was not primarily to unload inefficient, money-losing government tea estates, but to help develop an expanded and healthy national tea industry.

The Working Committee further proposed the following specific options for the consideration of His Majesty's Government. It should be further mentioned that not all of the options listed below are actually recommended for action. In fact, a couple should not be implemented. They are listed merely because they are options, albeit representing paths of action that should not be followed. The overall set of options is:

1. Reform and rehabilitate NTDC, but continue to operate it as a functioning state enterprise, or try to improve NTDC to the point that it could be privatized in two years or so.

2. Fully divest NTDC by selling or leasing it as a unit to the highest bidder or consortium of bidders.

3. Break up NTDC, selling the various commercial operations and properties separately, with the government retaining promotional, informational, research and extension functions.

4. Convert NTDC into a public limited company, floating shares on the still underdeveloped local market, with the intention of selling 10% of the commercial operations over as short a period of time as possible.

5. Break up NTDC, negotiating separate long-term leases for the various commercial operations and properties, with the government retaining promotional, informational, research, and extension functions.

6. Liquidate through public sale or transfer to other government agencies those NTDC entities and functions that have little potential for viability, or which serve little productive purpose.

TO THE PARTICIPANTS AT THE CFED SEMINAR

These are the options. Your team represents the government task force which will decide which course of action (or combination of courses) to take. You will be broken up into teams. Each team will present its decision to the full group, giving reasons for the conclusions and recommendations it has made. These presentations will be analyzed by the faculty and the whole seminar group. Remember to include an outline of a plan for carrying out the actions and decisions you have reached, including redundancy and social impact implications. Also, remember that the purpose is development, not dumping and that the NTDC case is the <u>first</u> major privatization transaction to be undertaken in Nepal.

Nepal Tea Development Corporation
Epilogue

Upon the recommendation of the working committee, the Asian Development Bank engaged a follow up consulting team to conduct a valuation and address some residual legal and accounting issues. By the time the valuation team arrived, the government had already made a determination as to how to proceed with privatization of the tea estates. The privatization decision is summarized as follows:

1) NTDC will be separated into two entities, consisting of a commercial entity which will operate the tea estates, and another entity which will be responsible for government activities to promote the tea industry in the private sector of Nepal.

2) The government will assume the outstanding liabilities of NTDC.

3) The government will sell shares in the new commercial entity to the extent of 49% of total ownership. 25% of the shares will be sold to employees of the tea estates and to small tea growers in the private sector. 24% of the shares will be made available for purchase by the Nepali public.

In addition to the three points specified in the decision, government officials indicated that it was the intent of the government to give the commercial tea operations complete autonomy, and allow it to operate without government interference. It was recognized that there was a need for additional technical assistance to make the tea estates competitive and profitable, and it was agreed that such assistance would be sought. However, there were no assurances that the government's stated intentions regarding autonomy or technical assistance would be carried out. Moreover, it was not the intent of the government to make any significant changes in the management of the commercial operations of NTDC.

The role of the valuation team was defined as follows:

1) Value the shares of NTDC that were to be sold.

2) Inspect physical assets and allocate them between the commercial tea operation and the promotional activity.

3) Assign values to all assets to initialize an accounting system.

4) Make recommendations on steps to be taken to organize the new company and issue shares of stock.

Conclusions of the Valuation Team

At the time the study was conducted, the financial condition of NTDC had become very dismal. During the study a check was made of NTDC accounts. It indicated creditors (accounts payable) of NRs. 18,317,683, while the company's bank balance stood at approximately NRs. 15,000. NTDC had been incurring increasing losses and had no funds or sources to meet its outstanding liabilities. If it were a private company, it would have declared bankruptcy long ago.

The valuation team concluded that shares in the commercial tea enterprise would have no value, and that a public issue of shares was not a viable option. The reason for this is that the company had not demonstrated any capability to operate profitably and provide a reasonable (or any) return on investment. If the commercial tea operations can be rehabilitated and made to operate profitably, at some future date it may be practical to sell shares.

A division of assets was made, with assets being designated for three groups: 1) assets to be included in the commercial operation; 2) assets to be transferred to other government entities; and 3) assets to be liquidated.

Group 1
Assets to be included in the commercial operation

Tokla Tea Estate	NRs. 61,510,000
Burnie Tea Estate	43,432,000
Kanyam Tea Estate	36,911,000
Ilam Tea Estate	11,952,000
Soktim Tea Estate	12,265,000
Buildings at Central Workshop	3,490,000
Head Office	9,636,000
Total	NRs.179,226,000
	US$ 8,070,000

Group 2
Assets to be transferred to other government entities

Chillingkot Tea Estate	NRs. 13,725,000
Outgrowers Scheme	370,000
Fuelwood Project	0
Cardamon Project	602,000
Total	NRs. 14,697,000
	US$ 660.000

Group 3
Assets to be liquidated

Baradasi Tea Estate	NRs.	500,000
Machinery at Central Workshop		1,664,000
Total	NRs.	2,144,000
	US$	96,000

Recommendations Regarding Management of the Tea Estates

The valuation team is in substantial agreement with recommendations made by the working committee regarding privatization of the tea estates. Current management is incapable of solving the problems confronting the tea operations. These problems are largely the result of control and management of the tea estates by the government. However, the government has made an irrevocable decision to retain 51% ownership in the tea estates, precluding most available privatization options.

The team strongly recommends that the government seek private companies to provide management of the tea estates on a long term contract basis. The term of the contract should extend for at least 15 years, so that the management firm will be motivated to pursue long term interests of the estate, perhaps at the expense of short term profit. An appropriate management contract will provide full autonomy to management and leave the government in the role of a passive owner. With such a contract arrangement the estates may reap the benefits of private enterprise while still being owned by the government.

Day Five Materials

The Privatization of Elektro, Inc.
Republic of Cula

Simulation Exercise

Introduction

The Republic of Cula, a country located in Africa, has recently mandated a large scale privatization program consisting of privatizing over 100 state-owned entities over the next five to seven years. Although the Government of Cula has strong political backing of privatization, implementation to date has been sporadic. Only fifteen small companies have been privatized so far. Although herald as a success (and has given the privatization program a tremendous boost) no clear strategy has been developed for the next groupings of privatization.

The World Bank was recently approached by the Republic of Cula for a large Structural Adjustment Loan. As a contingency for providing this loan, the World Bank wants to see real progress in the privatization program. The World Bank has set certain conditions on the privatization program, mainly that ten key companies must be privatized within a certain framework before the Structural Adjustment Loan will be released.

Elektro, Inc. is one of the ten companies slated for privatization in this grouping. The work completed on the privatization of Elektro Inc. by the Cula Privatization Commission (the body which oversees the privatization program) includes the following:

1. Company/Market Profile

2. Financial Analysis

3. Pre-Qualification Packages

Because of the quick turn-around required by the World Bank, most of the information was hastily gathered; however, it was deemed adequate for the bidder responses. The data for Elektro Inc. was compiled from publicly available information provided by the enterprise and from sources within the Ministry of Agriculture. None of the information has been independently verified. No audit has been performed on financial information provided and financial terms should be interpreted subject to limitations. No representation or warranty, expressed or implied, is made as to the accuracy or completeness of the information contained herein.

After careful review by the Cula Privatization Commission, two bidders pre-qualified. They include the following:

1. Sarus Operating Limited (SOL), currently a minority share-holder of Elektro Inc. (25% ownership). SOL is a

local company, with 15 years ownership in Elektro, Inc. They have good standing in the community and are known for quality work. They have been marginally profitable over this time period.

2. The Harvestors International Chemical Limited (HIC), a foreign firm based in Zurich, with no previous investment in Cula, or Africa for that matter. HIC has plants operating in ten countries worldwide with over $500 million in sales. They are well respected internationally and are considered very aggressive in market development.

As members of the Privatization Committee and of the two entities bidding (SOL and HIC), it is your responsibility to represent your organization and its interests in the privatization of Elektro Inc. Attached is information about the Republic of Cula, Elektro Inc. and its financial and operational condition.

Background Information on the Republic of Cula

Economic stagnation has existed in Cula for a number of years. The Government of Cula has imposed high import tariffs to protect national industries from foreign competition. Predictably, the result have been higher prices and lower quality of goods and services.

The losses created by the state-owned enterprises (over 100 companies) have contributed to increased domestic and foreign debt for the country. Government debts have become unsustainable.

The Government of Cula owns two agri-chemical processing companies, both with obsolete equipment, over-capacity plants, and an excessively large labor force that has a strong union backing and which demands unreasonably high wages.

Economic and Political Environment

"The Economic reform [in Cula] is a change of economic institutions and their relations. The goal of the economic reform is to accomplish the transition from government planned economy to a market economy. In contrast to the previous attempts at reform, the crucial issue of the day is not the improvement of the existing economic system, but a through-going transformation."[1] The reform project differentiates the chief reform measures in terms of two major categories: the establishment of the macro-economic framework. These include:

Transition of Zula to the Market Economy. Zula City: Institute of Economic Sciences, Charles University, 1990. p. 3

Macro-economic framework:

- stability-seeking financial, budgetary and monetary policies
- new tax system
- budgetary rules
- social policy measures
- price liberalization
- promotion of the growth of the private sector
- liberalization of imports

"The government seeks to imbue the economy with an identity of its own based on a unified commodity, labor, and currency market. Such reform should eschew any isolation from the international economy. In its contours and legislative backing, economic reform will pursue the goals of ever broader participation in integrating groupings - especially within the framework of neighboring economies."[2]

The most significant trends of structural policy will pursue concrete programs to achieve substantive goals in the following areas:

- lowering the power, raw-material, ecological and other exacting demands placed on production,
- strengthening the tertiary sector, including modernization of banking businesses, insurance companies and savings banks,
- privatization of state-owned assets,
- revitalization of economic growth and entrepreneurial activity in particular, private entrepreneurial initiative,
- development of foreign investment and tourism.

The parliament is working to clarify questions of private ownership, uniform legal statutes and remedies, development of a commercial and consumer banking system, uniform accounting standards, capital and investment banking market mechanism, and the collection/dissemination of statistical information on all aspects of the economy.

Social over-employment in Cula is estimated at between 15% and 25% of the labor force - 400,000 to 1,650,000 workers.[3] As with other companies, the remuneration system is based on a range of benefits.

IBID, p. 6

Brohumil Urban, "Towards Privatization in the Former Socialist Countries," presented at Economic Conference on Program of Transformation from a Centrally Planned Economy to a Market Economy, Zula City, December, 1990.

Under the emerging economic system, social conflicts generated by structural employment, liquidation of non-functional jobs, and social over-employment will be mitigated by a system of measures in which employment services will play a role of primary relevance.

Elektro Inc. Information:

Elektro Inc. is a producer of fertilizers and industrial chemicals for use in the local Cula market. To date, the enterprise has not been export-oriented [1% of 1990 sales, and 2% of estimated 1991 sales]. It has a significant domestic market share for its main products. The company's head office is in Middleburg, 80 km north of Cula City, the capital of the Republic of Cula. It has facilities at three other regional centers in Cula.

Market share per product group includes the following:

Product	Market Share	Growth Potential Next 5 Years
Assorted Fertilizers	75%	10%
Industrial Chemicals	75%	15%

The remaining market share for each category is held by Arch Rival Industries, a government-owned corporation currently slated for privatization in two-three years.

A preliminary assessment indicates that there is a potential export market to several European countries, if modernization occurs.

There are currently 1,280 employees who are considered moderately educated and possess the requisite skills for the firm's products. However, the country's full-employment policy over the past 35 years and the practice of non-effective over-employment produced low labor discipline and low labor productivity.

The company managers have worked hard over the last 30 years to make quality products; however the country's political and economic changes have brought not only new opportunities, but management challenges to meet the needs of clients operating within a market economy of choice and competition. Company managers will need intensive organizational development, finance, and management skills training if they are to compete effectively with producers in European and Asian markets.

Employment Breakdown

Title	Number	Avg. Compensation (Kcs)
Senior Managers	30	216,000
Middle Managers	75	125,000
Assistant Managers	150	55,000
Sales Force	50	45,000
Line Workers	550	15,000
Admin/Secretaries	275	8,000
Drivers, Misc.	150	5,000

A recent review of the company's operations was conducted. It appraised the fixed assets using a 'going concern' assumption. The fixed assets were appraised at Kcs 52,920,000 in excess of estimated depreciated book cost. For insurance purposes, fixed assets were estimated to have a replacement value of Kcs 85,000,000 in excess of depreciated book cost. The consultant also found that there are Kcs 26,500,000 accounts receivable in excess of 100 days and deemed them to be questionable; and that it is likely that the inventory is probably understated by 10%.

Very little new product research and development has occurred in the past, as government set production quotas and direct product innovation and invention through government-financed research institutes which employ the majority of the country's agricultural and chemical scientists.

However, recent talks with research consultants, Electro Inc. managers are considering an investment in the "next generation" of agri-chemicals currently being developed. It is estimated that these products could increase sales by 10% at gross profit margins of 32%, and using existing production facilities which were frequently idle during the past years. The production machinery uses technology developed 20 years ago, and it is quite difficult to consistently produce high-quality products.

Managers are now working with consultants and foreign machinery representatives to consider state-of-the-art production equipment. This equipment may require a capital investment Kcs. 30,000,000 - Kcs 50,000,000 each year for the next five years. Managers expect this will reduce unusable materials by 10% of production [using existing machines, error rate would be about 20%], and cut labor costs by 15%. If existing products and new equipment output match industry quality standards, Elektro-Inc. managers expect their lower labor rates and central shipping location could give them a strategic advantage in serving foreign markets.

Elektro Inc. managers are not available to talk with you. However, general questions can be answered by the consultant advisory committee.

Exercise Task

The participants will be divided into three groups. One group represents the Republic of Cula (the Privatization Committee), one group represents SOL, and one group represents HIC.

The two private sector firms have been pre-qualified for final bidding. In the absence of a written document, the Cula Privatization Committee has asked each firm to make an oral presentation outlining their key points. Although price is an important component, the government recognizes that other objectives must also be met. A successful offeror should take these other issues into consideration.

In the first meeting, each group will have an opportunity to develop their specific strategic positions. After that, each private sector team will make a brief presentation to the Cula Privatization Committee, followed by a question and answer session. Following that, each team will caucus in separate groups, and then make a final presentation to the Privatization Committee.

A general debriefing on the case discussions will follow.

The objective of this exercise is not the determination of a winner per se but rather for each group to have a better understanding of what the parameters are for a negotiation process. Because of time limits, this exercise is necessarily simplified, however, the key strategic points will be addressed.

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Private Sector Bidders

Sarus Operating Limited (SOL)

Included below are items known only to your company. Because of your long history in Elektro, Inc, you feel confident of winning the bid. You do feel uncomfortable, however, because your competitor is a large international firm with tremendous market opportunities; items SOL does not possess. Additionally, in a agreement signed by your President, if the Republic of Cula sells their shares, then the purchasing entity has an option to purchase SOL's 25% stake.

This is especially troubling to SOL because Elektro, Inc. represents 60% of SOL's earnings and 40% of SOL's employment base.

You do, however, have tremendous advantages over the competitor and must utilize those to the maximum in your bid negotiation strategies. Therefore, you must focus on your company's strengths in your negotiations as well as be responsive to the government's concerns.

In preparing your negotiation strategies, consider the following items:

1. Impact of privatization on the Cula economy.
2. Impact on employees.
3. Impact on management.
4. Addressing the concerns of the Rupublic of Cula
5. How financing will be arranged, and in what breakdown.
6. How do you envision the growth of Elektro Inc. (short and long term development plans)?

Guideline Parameters:

1. You have been authorized to bid as high as Kcs. 280,000,000. Pay attention to other hidden costs.

2. You are authorized to offer severance packages, if necessary, up to Ksc. 15,000,000

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Private Sector Bidders

Harvestor International Chemical Limited (HIC)

Included below are items known only to your company. Because of your international expansion plans, this project looks ideal for expansion into Africa. Your Board of Directors, however, are not so sure, because of the possible unknown risks involved. Your Investment Advisory Committee has advised them otherwise, and you have been given a confirmation to bid for the project.

You are, however, at a disadvantage to your competitor because of your lack of expertise in African and, especially Cula's market. Therefore, you must focus on your company's strengths in your negotiations as well as be responsive to the government's concerns.

In preparing your negotiation strategies, consider the following items:

1. Impact of privatization on the Cula economy.
2. Impact on employees.
3. Impact on management.
4. Addressing the concerns of the Rupublic of Cula
5. How financing will be arranged, and in what breakdown.
6. How do you envision the growth of Elektro Inc. (short and long-term development)?

Guideline Parameters:

1. You have been authorized to bid as high as Kcs. 260,000,000. Pay attention to other hidden costs.

2. You are authorized to offer severance packages, if necessary, up to Ksc. 20,000,000

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Cula Privatization Committee

This is an extremely tense time for your Committee. The Office of the President is screaming at your office because they need the Structural Adjustment Loan. The Unions are organizing a major protest, in that it is anticipated that jobs will be lost in the privatization; and the public at large is worried that you will "give away" the enterprise.

In addition, you have selected two bidders with very different backgrounds; yet both have very important strategic implications.

Your responsibility is to develop negotiation parameters for the Republic of Cula based on a check list of objectives. This list you must develop as a group. Consider both short and long-term issues/implications in your analysis as you develop your strategy.

As a floor price, you cannot award a bid that is below Ksc 250,000,000.

MEMORANDUM

TO: Margaret Pope
POL/CDIE/DI Acquisitions
SA-18, Room 303

FROM: John J. Wiebler
Program Officer

DATE: July 23, 1993

SUBJECT: USAID/Zambia Documents

Enclosed USAID/Zambia is forwarding the following for use by A.I.D.'s Center for Development Information:

1. Privatization Strategies and Techniques: Instituting Practical Methodologies. May 10 - 28, 1993

/c.c.