

24942



D R A F T R E P O R T
O F T H E

**SENIOR POLICY WORKSHOP ON
IMPROVING THE PERFORMANCE OF
PUBLIC ENTERPRISES IN AFRICA**

Held at
**Ethiopian Management Institute
Debrezeit, November 12 - 16, 1990**

Organized by
**United Nations Economic Commission for Africa
Special Action Programme in Administration and Management (SAPAM)**

**REPORT ON SENIOR POLICY WORKSHOP
ON IMPROVING THE PERFORMANCE OF PUBLIC
ENTERPRISES IN AFRICA**

I. BACKGROUND AND INTRODUCTION

The participants of the Senior Policy Workshop on Improving the performance of Public Enterprises in Africa met at the Ethiopian Management Institute Training Center in Debrezeit, Ethiopia from November 12-16, 1990.

The Workshop was attended by about 30 participants representing 17 countries, representatives of the International Center of Public Enterprises in developing countries in Ljubljana, Yugoslavia, and UNIDO as well as Secretary the General of the African Association of Public Administration and Management

The workshop's broad aim was to facilitate the exchange of experiences of modalities for the improvement of the performance of public enterprises in Africa. The specific objectives of the workshop were to:

- (1) Identify and analyze the constraints to efficient and effective management of the Public Enterprises;

- (2) Examine how policies and practices of the supervisory authority (owner management) impede or facilitate the performance of Public Enterprises;
- (3) Analyze the option of commercialization of public enterprises;
- (4) Examine the mechanisms for enhancing financial viability of public enterprises;
- (5) Examine and suggest policies, measures and procedures for improving the productivity and efficiency of public enterprises; and
- (6) Propose a system of performance indicators to be used for monitoring, evaluating and improving the performance of public enterprises.

The workshop was officially opened by H.E. General Afework Atlabachew, Vice-Minister of Industry of the Peoples Democratic Republic of Ethiopia. Dr. Sadig Rasheed, Chief of Public Administration, Human Resources and Social Development Division of the Economic Commission of Africa (ECA) welcomed the participants to the workshop on behalf of the Executive Secretary of the ECA and himself.

In his welcoming remarks to the participants, Dr. Rasheed stressed the significance of the public enterprises in African economies and that they have to be more effective and efficient if they are to contribute to Africa's economic recovery and development. He challenged the participants to seriously address the problems currently faced by African public enterprises and prepare concrete recommendations to deal with them.

In his keynote address to the participants, the Vice-Minister of Industry emphasized the topicality and relevance of the theme to present day Africa and argued that public enterprise will continue to play a significant role in African economies in spite of the antipublic enterprise mood that is currently prevalent. Having Reviewed recent economic reforms launched by the Peoples Democratic Republic of Ethiopia, he called upon the participants to address a number of issues and problems associated with current practices in public enterprises in Africa. The participants found the two speeches useful as they set the tone for their subsequent deliberations by identifying the major difficulties in public enterprises management in Africa.

The workshop participants have benefitted immensely from the working papers presented in the workshop by noted African Scholars and representatives of international organizations. The presentations on country experiences proved useful in enriching and reinforcing the issues raised and the points made by the working

papers. Participants were struck by the similarities of problems being experienced in the different countries. The exchange of experiences on the efforts made to cope with the problems in the different countries were found instructive and useful.

During the course of the deliberations, the participants made the following observations.

- (i) Enchantment with public enterprises as instruments of socio-economic development in the immediate post-independence years has given way to considerable disappointment and skepticism about their performance, leading to greater emphasis on the need for privatization and/or improvement on the performance of public enterprises in the 1980s.

- (ii) The dire economic situation of African countries since the beginning of the 1980s has led to a serious examination of the proper role and scope for government intervention in economic activities. At the heart of that reconsideration has been the public enterprise, given that it is the primary vehicle through which governments have participated or intervened in various economic activities and the considerable financial outlays that governments have spent and the losses that they have had to absorb in support of public enterprises.

Thus, as the economic crisis of African countries worsened, leading to adoption by them of stringent structural adjustment or economic reform programs, privatization of public enterprises and/or measures to improve the performance of more enterprises that still remained in the public domain have been vigorously advocated by bilateral and multilateral donors and actively pursued by African countries.

In these circumstances the need to improve public enterprise performances is assuming considerable importance and requiring urgent attention.

- (iii) A key reason is that public enterprises in Africa make claim to significant public financial resources, whether such claim is judged by the size of direct and indirect government subsidies to their enterprises or losses which the governments normally have to cover. Such a drain on public financial resources can hardly be justified, particularly at a time when African governments are facing a major economic crisis and overall shortage of financial resources. That being the case, it is important that the public enterprises should not become a burden on the national budgets.

- (iv) Another reason the participants noted for the drive to improve public enterprise management and performance is that the public is best served when public enterprises produce their goods and services in an economically efficient manner (cost-minimizing methods).

- (v) Finally, there was a consensus among the participants that regardless of the drive to privatization, public enterprise will continue to be a significant sector in the economies of a number of African countries. Given that, public enterprises should be able and should be made to contribute effectively to accelerated growth and development and should indeed, as much as possible, generate surpluses and profits. Ways and means should be found to make them operate effectively and efficiently and to generally become economically viable entities.

If public enterprises are to assume a more vigorous role in the economies of the respective African Countries and contribute to the recovery and development efforts underway, it is important that the critical issues and areas that need to be improved be identified, diagnosed and appropriate remedial measures prescribed.

In the course of their deliberations, the participants noted:

- (a) that it was necessary to identify the challenges to public enterprise performance in the 1990s. An assessment of the environmental constraints and challenges will make it possible to come up with realistic proposals for dealing with them.
- (b) It was also felt necessary to critically examine the Government Enterprise relations and remove those constraints that affect the effective performance of Public Enterprises.
- (c) It was also noted that in many African countries public Enterprises are under immense pressure to privatize. Mostly such pressures are externally initiated or imposed. While the participants did not see anything wrong with privatization in as far as there are justified cases for it, they nevertheless felt strongly that privatization decisions should not be regarded as panacea for all ills. Public Enterprises can be made financially viable by creating an enabling environment that would make it possible for them to perform more effectively and efficiently. The participants felt that policy measures and options that conduce to better Public Enterprise

performance will have to be tried first before resorting to privatization. To this end, the participants thoroughly examined policy measures and options that could be tried out to enhance financial viability of public enterprises.

- (d) Any improvement in performance of Public Enterprises could not be realized without appropriate human resources development strategy. The participants addressed this issue at length to determine proper strategies that could be mapped out to that end.
- (e) Participants recognized the importance of continuously monitoring and evaluating the performance of Public Enterprises in Africa. However, such action presupposes the existence of appropriate criteria to assess the performance of public enterprises. Developing appropriate performance parameters and installation of suitable managerial and financial Management information systems were considered as areas requiring urgent attention.
- (f) Another area that the participants focussed attention on was maintenance management. They examined the existing constraints to improved maintenance management and made recommendations for improvement and implementation.

II. OBSERVATIONS AND RECOMMENDATIONS

Having dwelt at length on the above factors that condition the performance of public enterprises in Africa, the participants of the Senior Policy Workshop on Improving the Performance of Public Enterprises in Africa at Debrezeit, made the following observations and recommendations.

A. Challenges of African Public Enterprises

The participants reviewed the development of public enterprises in Africa since independence and noted that the expansion trends that characterized the first two decades are on the decline. It was also observed that the poor performance of public enterprises have tended to obscure their very many positive contributions to laying the foundation for industrial and infrastructural development of African Countries. Public Enterprises, for instance, have been major vehicles for construction and expansion of telecommunications, energy facilities, water, health, roads, education and technology.

The decade of the 1980s was characterized by an international economic environment which was particularly hostile to the efficient and effective performance of Public Enterprises leading to various pressures for reforms of African Public Enterprises.

The hostile international environment was reflected in pressure for devaluation; external lending restrictions; high international interest rates; low export earnings; high input prices; severe debt service pressures; unfair trade practices such as various forms of protectionism; pressure for trade liberalization which often resulted in reduced market share and revenues; etc

Additionally, Public Enterprise performance has been severely constrained by internal factors such as multiplicity of control and supervising agencies; restricting legal codes that prevented public enterprises from profitable diversification; inadequate autonomy limiting the decision-making space of public enterprise managers; absence of adequate incentives required to revitalize the work force of African Public Enterprises and high corporate tax requirements etc.

Looking ahead, the participants identified a number of challenges that will confront Public Enterprises in Africa in the next decade. First, is the liberalization of economies and promotion of competitive markets that are global imposing on African Public Enterprises the need for allocative efficiency. Second, the budgetary position of most African governments will continue to provide very limited room for manoeuvre. Only in most exceptional cases will African governments be able to underwrite the losses of public enterprises or pursue policies which require subsidies. Third, a world wide trend towards regional trading

blocks has become discernible. This is the context in which Africa must develop and promote traditional exports.

The above constraints could present a number of opportunities in as much as they are well-handled. Among these are opportunities to turn around poor performing companies and wrest further autonomy, to exhibit innovations, competitive spirit and develop aggressive entrepreneurial skills, and to cope with turbulent business environment through adaptation of appropriate management information systems and technology.

B. Government Enterprise Interface

(i) The Autonomy-Control Dilemma

In examining the government enterprise interface, the participants addressed the issues of balance between autonomy and control, responsibility for policy decisions on critical macro economic issues such as prices, wages, investments, and borrowing as well as accountability.

It was observed that the proper balance between autonomy and control of public enterprises by government lies in identifying the role and responsibility of government first as regulator and second as owner of public enterprises.

Through its legislative and executive authorities, government sets the rules and regulations governing the conduct of business. This includes areas such as taxation, sales and excise taxes, issues relating to the companies law, Act or Code and the various instruments of incorporation of public enterprises.

As owner of the investment in public enterprises, government has the legitimate right to determine the objects and policies of the company as well as the right to determine how the company should be managed. Indeed government can reserve the right to run the business as part of the government machinery. However, even though some government departments conduct activities which are business in nature, government has chosen to locate the conduct of business of public enterprises outside regular government departments. The issue therefore is which of the legitimate rights related to the conduct of business by public enterprises does government wish to delegate, and by how much?

Participants expressed the view that government if it accepts that public enterprises should conduct business in an enterprising manner with a profit motive, and if public enterprises are to compete successfully in highly volatile business environment, there will be the need to delegate to public enterprises sufficient authority to pursue the responsibilities and objectives.

The management structure of private enterprise which should serve as model for government is recommended considering there is irrefutable evidence that it has been tried successfully for a long time. What then is the structure that private enterprise pursues? This structure derives from the clear distinction of two clear functions. It was observed that one function was policy formulation for the conduct of management in the day to day administration of the business and the other function the daily management of the business.

The first is normally delegated to a group of highly motivated professionals with proven business acumen preferably with a mix of expertise related to the peculiarity of the business. This group of professionals constitute the board of directors. The board has the responsibility normally to appoint and remove the chief executive as well as to formulate company policy governing all sections and activities of the company. The shareholder appoints the board and has authority to remove the board. The control of the shareholder therefore is exercised through this authority at annual general meetings or emergency meetings as the shareholder may determine. The management, however, has operational control of the company.

It was observed that just as the balance between autonomy and control is entrenched in the clear definition of responsibility and appropriate authority required to conduct the business of the board

and management in the case of private enterprises; that clarity of definition can be used to induce the public enterprise management with the same **modus operandi**. To buttress this practice the various companies codes of many countries provide for sanctions against board members and management individually and collectively. The real balance however can be achieved through **discipline and management competence which will foster respect and cooperation**.

Having made the above observations, the participants wish to urge governments to follow the private sector practice by establishing boards of directors and delegate authority equivalent to their counterparts in the private sector. A government with the power to regulate, legislate and even expropriate property of companies, individuals etc. need not fear delegation of authority so long as there is sufficient room to monitor the activities of the board, management in the operations of the business.

(ii) **Decision-making arrangements for macro-economic issues: prices, wages, mix of products, services, borrowings and investments.**

The participants felt that the board should be entrusted with the control of policy in such areas as prices, wages, goods and services like its counterpart in the private sector. The board can hardly neglect the market signals that affect the above issues without dire consequences. However, the issues of new investments

or borrowings will need the approval and guidance of the government in the same manner that annual general meetings decide on the issues in the case of the private sector.

C. Enhancing Financial Viability of Public Enterprises:
Policy Measures and Options

In examining the financial situation of Africa public enterprises, participants noted the following characteristics: low or negative profit, low or negative rate of return on investments; under capitalization, excessive borrowing, absence of indicators to monitor the financial health of enterprises, negative and declining trend in growth of assets, absence of financial management system resulting in financial undiscipline.

The participants observed that this trend which has adversely affected the financial viability of many public enterprises has to be addressed if these public enterprises are to be able to contribute to growth and recovery in African countries.

In the course of the deliberations, participants debated whether commercialization could be viewed as an alternative to privatization. They took the position that commercialization was inherent in the concept of business-oriented public enterprises. As such, commercially-oriented public enterprises should act as private enterprises that make profits.

Having made the above observations, the participants recommended that:

1. That there should be conscious acceptance of financial profitability as non-conflicting public enterprises objective. It is important to make policy makers and managers aware that financial profitability is a necessary goal to pursue in management of public enterprise to enhance generation of savings, capital formation, and ensure return on investment to the nation.
2. Return on investment must be consciously planned, pursued and monitored by managers; and public enterprise management involves financial management responsibility for recognizing financial profitability as worthy social objective.
3. The above entails that public enterprises should have management autonomy for self-managing of resources and deciding on financing sources with minimum outside interference in order to critically discern responsibility and avoid ascribing poor financial performance of public enterprises to discharging of social objectives or external burden.

4. There is a need to determine adequate capital structure at least in terms of wise financial management decisions that lead to judicious use of leverage (debt/equity mix, and working capital management. This needs monitoring of capital mix and profitability through application of modern principles and practices of finance, and financial analysis of ROCE, debt/equity ratios and deciding of fixed and working capital proportion).
5. Modern business techniques should be applied for identifying "financial distress" conditions and/or predicting impending "enterprise sickness" in public enterprises through the use of appropriate financial ratios and taking concrete steps towards creating measures for their implementation.
6. There is need to identify criteria for determining sick and potentially sick public enterprises through acceptable financial index.
7. Adopt accounting tools for analyzing financial profitability and monitoring and predicting financial health of public enterprises.
8. Enhance the financial viability of public enterprises in Africa by restructuring the capital of public

enterprises. One way of changing the financing mix would be to increase the equity base not only by increasing government fund, but also by increasing public participation in equity. Other means would involve improving financial profitability and liquidity through merger and consolidation of enterprises.

9. Devise new approach of financial reporting standards in accounting classification, valuation, and income determination for public enterprises which include consideration of effect of social costs or external burdens on enterprise financial profitability.
10. Improve mechanisms for timely preparation of financial statements.
11. Devise special financial performance indices appropriate for measuring profitability.
12. Develop comparative standard ratios for analysis of public enterprises in different lines for industry in Africa.

D. Human Resources Development Strategies for Enhanced Capacity of Public Enterprises

Participants recognized that recruitment, education and training functions are critical to success of poorly performing African public enterprises. Participants also noted that management styles and approaches do influence performance of enterprises. Similarly it was observed that the absence of package of incentives for management is seriously constraining the performance of public enterprises. As a result of the above factors, many public enterprises suffer from acute shortage of qualified managers; politically-motivated recruitment, and lack of organized human resource audit system.

Having made the above observations, participants recommend as follows:

- (i) Managers should be recruited on the basis of qualifications and experiences relevant to the positions to be occupied. In this regard, merit based recruitment process should be strictly adhered to.

- (ii) Education and training of public enterprises managers must be geared to the technical requirements of the job and should equip managers

with skills to analyze internal and external influences on the performance and productivity of public enterprises.

(iii) Effective human resource audit system should be installed.

(iv) Regional data banks of public enterprises' managers should be developed and installed.

E. Strategies for Performance Improvement

Participants observed that public enterprises in Africa are constrained internally by lack of motivation, low productivity, inadequate managerial skills, absence of automated accounting system, ineffective planning and control, inadequate management information, over-staffing, poor technological base, and ineffective recruitment system.

The participants also identified the following internal constraints to effective performance of public enterprises: lack of clarity of objectives, multiplicity of supervising agencies, excessive politically motivated appointments and under-capitalization.

To remedy the above constraints, participants recommend that governments should:

- (i) clarify objectives of enterprises, specifying whether they are profit or non-profit making;
- (ii) streamline and reduce the chain of commands;
- (iii) allow management authority;
- (iv) appoint managers on the basis of merit.

F. Guideline for Evaluating Performance of Public Enterprises

Participants emphasized the urgency for developing parameters for assessing and monitoring the performance of African public enterprises.

In this connexion, they recommended the use of certain key performance indices for assessing of African public enterprises, such as general performance indices, management performance indices, and financial performance indices. The participants suggested the application of the following indices:

- (i) profit related to capital employed;

- (ii) net profits after taxes related to net worth;
- (iii) gross profits to sales;
- (iv) sales related to capital employed;
- (v) sales related to fixed assets;
- (vi) sales related to current assets;
- (vii) sales related to stocks;
- (viii) sales related to debts;
- (ix) current assets to current liabilities;
- (x) liquid assets to current liabilities;
- (xi) gross added value related to fixed assets;
- (xii) gross value added related to number of employees;
- (xiii) sales related to number of employees.

G. Maintenance Management for Enhanced Public Enterprise Productivity

Participants observed with dismay the total negligence of maintenance in many African public enterprises. Managers do not seem to recognize that much profit can be generated from effective maintenance, just as colossal losses could be sustained from its neglect.

Participants noted with satisfaction some of the efforts underway in a few African countries to install and develop maintenance management systems to good advantage.

Participants identified a number of constraints to effective maintenance systems in African public enterprises viz: machinery and plant maintenance being carried out on "fire-fighting" basis, poor management system, lack of skilled manpower, lack of incentives for maintenance personnel, wrong attitude of managers towards maintenance and lack of spare parts and tools, purchase of machinery and spare parts on criteria that do not take life-cycle cost into account.

To overcome these constraints, participants urge African public enterprises to install and sustain a planned maintenance system, to purchase machinery and spare parts taking life-cycle cost into account and develop an appropriate incentive packages for maintenance personnel.