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Broadening Local Participation in Privatization of Public Assets in Africa

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Executive Summary

Since the mid-1980's, privatization has been the central issue of the development agenda as several African countries underwent structural adjustment programmes. However, because of institutional and limited savings capacity factors, local participation in privatization has been significantly low. High political instability and economic uncertainty, coupled with crowding-out of government ownership has discouraged firms and households from holding financial assets. Despite the expressed desire of many African governments to broaden ownership of indigenous investors, with very few exceptions, methods that broaden local participation have not been commonly used. Nevertheless, privatization has been on the rise and acceptance of the need to reduce the size of public enterprises has grown.

The study begins with an overview of the trends in privatization in Sub-Saharan Africa in the last decade and half. Against this background: First, the study focuses on review of the issue, the rationale and the problems associated with broadening local participation in privatization, including the difficulty encountered in reconciling equity with corporate governance within the African context. Second, selective methods that broaden local participation are concisely discussed. These include management and employee buyouts, employee share participation, directed group ownership, public flotation and financial intermediaries. Moreover, because of the major linkage between privatization and stock markets, a section of the paper discusses the different stages and nature of development of African stock markets. Third, country-specific efforts and outcomes in broadening local participation are analysed. The countries and methods include Burkina Faso (consortium of local and foreign investors), Cape Verde (a participatory approach), Kenya (a politically acceptable ownership), Uganda (directed group ownership), Zambia (privatization trust fund), and Zimbabwe (Unit trust).

In the road ahead section, as a long-term solution to privatization in general and broadening local participation in particular, the study indicates the need to improve the process, the need to activate mass privatization and the importance of creating a conducive investment climate. As a medium-term solution to broadening local participation, replicating 'best practice' of directed group ownership is analyzed using different scenarios. First, the paper argues that in all the major procedures in improving the process of privatization, namely, securing consensus, ensuring transparency, investing more on design and preparation and ensuring appropriate institutional blocks,

the objective of broadening local participation reinforces the whole privatization process. *Specifically, broadening local participation in privatization secures consensus of the general public, helps to depoliticize and speed up the process, indicates a strong commitment to transparency and sends an encouraging signal to foreign investors*. Second, acknowledging the difficulty involved in designing and implementing mass privatization through voucher schemes in Africa in the short term, the study points out that with a strong commitment and planning, it could be achieved at least in the long-term. Third, as a prerequisite for promoting investment and acquiring credibility with both foreign and indigenous investors, continent-wide efforts are emphasized to ensure stability and to improve the investment environment.

In conclusion, while the study builds on the fact that privatization and stock market development are inextricably linked and mutually reinforcing, and recommends it as a long- term solution to broaden ownership; it also goes to recommend that the method of directed group ownership as ‘best practice’ should be implemented as a medium-term solution concurrently with stock market development for an optimal path to broaden local participation in privatization of public assets.

I. Introduction

1. Since the mid-1980's, privatization has been the central issue of the development agenda as several African countries underwent structural adjustment programmes. However, because of institutional and limited savings capacity factors, local participation in privatization has been significantly low. High political instability and economic uncertainty, coupled with crowding-out of government ownership has discouraged firms and households from holding financial assets. Despite the expressed desire by many African governments to broaden ownership of indigenous investors, methods that broaden local participation, such as management/employee buyouts, have not been commonly used in Africa. Nevertheless, privatization has been on the rise and acceptance of the need to reduce the size of public enterprises has grown. By the end of 1996, around 2,700 privatization transactions with a total sale value of $2.7 billion had taken place in Sub-Saharan Africa (see Table 1). Up to 1996, emphasis was primarily on divesting small and medium-size enterprises. However, with attention focusing more on the larger enterprises, including several privatizations in the telecommunications sector, a significant increase in the value of the deals concluded is expected.

2. At the beginning of 1990, about a dozen countries in Africa had undertaken some form of privatization; by 1993 that number had doubled and by end 1996 all but five countries had divested some public enterprises. In terms of the number of transactions, most of the privatization activity has been concentrated in a few countries. Of the 2,689 reported privatization transactions that took place between 1988 and the end of 1996, 1,430 were concentrated in just ten countries (see Table 3). In terms of sectoral distribution, privatization has occurred most often in the manufacturing and industrial sectors, which is about 30 percent of transactions. Enterprises involved in agriculture, marketing, and processing accounted for 23 percent and transactions in service industries for 22 percent. Transactions involving financial institutions accounted for less than 5 percent.

3. There is no correlation between the number of transactions and the sale values of privatization in Africa. Looking at the number of transactions alone, as an indicator of the extent of privatization is misleading because of the typically small size and low values of the enterprises divested. For example, 191 transactions in Ghana yielded more than $400 million, whereas 548 transactions in Mozambique yielded only $179 million (see Table 3). In the period 1990 to 1996, only 12 countries reported transactions totalling

more than $50 million and only 9 countries had sales totalling more than $100 million. The value of transactions has been the highest in South Africa, where privatization of two major enterprises yielded $762 million. Most transactions involved small to medium-size firms. Of the 1,259 transactions, as many as 472, 37 percent involved sales of less than $100,000. A few transactions have accounted for most of the privatization sales value. The top 20 transactions totalled around $950 million, and of that total, transactions in South Africa and Ghana together accounted for $445 million, or almost 47 percent (see Table 2).

4. Wide range of different methods of privatization is used in Africa. In the early 1990's, *liquidations* were the most commonly used form of privatization, followed by *competitive sales of shares.* By end 1996, 16 methods of privatization had been employed in Africa, with 32 percent of all transactions involving the sale of shares by *competitive tender*. Not all sales of shares are open and transparent. In Angola, Ghana, and Senegal, there are many examples of shares being sold directly to foreigners. In Kenya, shares were sold to existing shareholders with pre-emptive rights. Some assets sales have also been handled on a non-competitive basis, which has led to accusations of lack of transparency. In many countries, including Ghana and Kenya, it is difficult to know how many bidders participated in competitive processes and what selection criteria were applied. The number of enterprises being privatized through indirect methods, such as lease arrangement and management contracts, is on the rise; but their use is not widespread. Because such indirect methods are most often used in the privatization of utilities, the low usage of these methods underscores the extent to which utilities in Africa remain in the public sector. A significant increase in direct and indirect means of privatization of utilities is expected in the near future.

5. Prior to privatization, African governments owned the majority equity in over 80 percent of the enterprises that were subsequently the subject of privatization transactions. Following privatization, the governments retained no ownership in at least 70 percent of all privatized enterprises. The governments had maintained a majority ownership in only 6 percent; and 10 percent of transactions resulted in minority government ownership. In some cases, shares remain in government ownership with a view to subsequent public flotation once the capital market develops. For this purpose shares in enterprises in Zambia are held by the privatization trust. In other cases the rationale for government retention is unclear. For example, the governments in Ghana and Kenya continue as partial owners of some privatized hotels. Changes in ownership usually provide a good picture of the degree to which the government is willing to relinquish its involvement in a particular sector. In Zambia, Togo and Benin the governments were willing to reduce

ownership share to zero in more than 85 percent of the transactions. In Zambia the total percentage of firms in which the government exited fully was an impressive 98 percent. At the other end of the spectrum is Burkina Faso, where, in most cases, the government did not divest fully, preferring instead to retain an equity interest in more than 60 percent of the enterprises.

6. In general, the economic benefits of privatization are now widely accepted, and include: improving enterprise efficiency and performance; developing competitive industry; accessing capital, know-how and markets which accelerate growth; achieving effective corporate governance; development of well-functioning capital markets; and, securing optimal price for the sale. In the process of privatization, each stage involves balancing economic and political goals. The process is also shaped by the specifics of the business involved and country economic circumstances, particularly those relating to the stage of development of the domestic capital market. These factors determine the institutional framework and approach of the whole privatization program. At each point, the keynote is political transparency. Transparency maximizes popular perception of fairness and strengthens support for privatization. There is an abundance of literature on the framework of privatization as a whole. For a thorough analysis of the principles and practices of privatization see Donaldson and Wagle (1995).

II. Broadening Local Participation

2.1 The issue

7. Broadening ownership is frequently cited as one of the objectives of privatization by African governments, but with few exceptions, only minor efforts have been made in this direction. Public offerings and some directed group schemes have given some Africans the opportunity to invest. At the enterprise level, some management buyouts and employee participation have also extended ownership to more individuals. However, much more needs to be done to reach a significant number of the population that has no or little savings, and is therefore unable to participate in privatization under the methods currently employed.

8. Although broadening ownership is cited as one of the main governments' objectives of privatization in Africa, there is overwhelming evidence that other factors have influenced privatization.

9. If broadening ownership had been a principal objective, it would not have been expected to see so many sales of investments in companies with existing shareholders having pre-emptive rights or sales on non-competitive terms to foreign investors. For example, in Kenya, over 70 percent of privatization transactions up to the end of 1995 were pre-emptive rights. Of 110 completed privatization transactions in Kenya, between 1991 and 1995, excluding Kenya Airways, nearly 73 percent involved non-competitive methods.

10. If one of the major goals of privatization had been to broaden ownership, there would have been less emphasis on maximizing sale values and more emphasis on local participation. In fact, considerable time and resources were devoted to valuations; and price was the single most important determinant in selecting investors in most cases. Selecting a bidder who offers the highest price renders it easier to convince observers that the process is transparent and thus provides political protection. However, it has often served effectively to exclude indigenous investors.

11. Although transparency has improved over time, the privatization process in many African countries continues to be insufficiently transparent. The cloud surrounding some transactions, especially those handled outside privatization agencies, strongly suggests the presence of vested interests.

12. Objectives of individual transactions are never stated. Sometimes they may be deduced, but often they remain unclear.

2.2 The rationale

13. Broadening local participation in privatization satisfies national aspirations; it can also activate political acceptance of privatization, and ultimately, it can boost domestic savings. In many countries, the fear of 'economic neocolonialism' through privatization is a powerful force against foreign investment. At least in principle, privatization that results in some private ownership by indigenous citizens is more acceptable than outright sale to foreign investors. Since independence, African governments and donors have invested heavily in public enterprises, and these institutions are rightly regarded as public assets. The public perception of the major public enterprises tends to overestimate the actual performance and value of these institutions; and governments, for political reasons, have been reluctant to inform their constituents how poorly most public enterprises have performed. Moreover, it is more embarrassing when these enterprises have substantial debts guaranteed by their governments. Given the above, it is therefore understandable that there is a strong desire for sovereignty and for the benefits of privatization to be enjoyed by the people, if privatization must take place at all. Nevertheless, although broadening local participation is challenging, it is important if privatization is to gain the necessary political acceptance. In addition, as privatization reaches a wider spectrum of the public, it can help to promote transparency.

2.3 Problems associated with broadening local participation

14. Although broadening local participation is a legitimate objective, when the subject of broadening local participation is discussed, heated disagreements arise. First, resentment against relatively prosperous ethnic minority groups and foreign investors comes to the surface. Second, political differences and perceived nepotism of groups identified with one or more tribes are believed to benefit from opportunities that are not open to all. Nevertheless, heated debate is not surprising when ownership facts are not disseminated, and when the large majority of the population is poor and unable to buy shares in firms being privatized. Therefore, despite the political need to meet the desire of indigenous people to broaden ownership, governments often prefer to involve a foreign strategic investor. Foreign investors bring with them new investments, proven managerial capabilities,

and new technology. Selling to a foreign investor is also often the only way to avoid accusations of nepotism or tribalism. For example, in Ghana and Uganda, this has occasionally been the factor behind sales to foreigners.

15. Several attempts have been made to increase local participation in privatization. In order to assist local investors, virtually all countries have negotiated deals with citizens for payment on deferred terms. Unfortunately, credit administration has been difficult with privatization agency personnel who are too busy with current transactions to monitor and take action to collect payments due on past deals. Moreover, credit approval has proven problematic because many buyers have failed to meet the repayment schedule. Two factors have contributed to these defaults. First, in preparing their bids, local investors have not always given adequate consideration to the requirement for investment and working capital in addition to that needed for purchase. This same mistake has often been made in evaluating those bids. Second, in some instances, the buyers did not have the financial resources they claimed to have. In Uganda, for example, deals negotiated with nationals that provided payment on deferred terms were backed by bank guarantees. In most cases, the buyers failed to meet their payment obligations, and the privatization agency had to call on those guarantees. Although the problem of recovering the amounts due has been transferred from the agency to the banks, the experience led the privatization agency to decide in early 1995 that single-payment sales should be given preference. Thus, the experience with credit sales poses a dilemma. On the one hand, all-cash deals avoid the risk of default and the burden of credit administration. On the other hand, a lack of credit effectively excludes a majority of local investors and runs counter to the aim of broadening local ownership. Equity calls for returning of the public assets to the people at large, which implies distribution of property independently of the ability of individuals to pay; while corporate governance, in contrast, requires owners to have effective control over the enterprises. Therefore, reconciling these two contradictory objectives of equity with corporate governance is the main challenge that African policy-makers must deal with as regards to privatization in Africa. One possible positive effort to reconcile these two contradictory objectives is to involve the people in the early stages of the privatization process by providing information and by encouraging debate. Most importantly, people need to have a clear understanding of the context in which indigenous investors can participate.

2.4 Methods for broadening local participation

16. Methods that could be used to broaden local participation or ownership range from those that provide opportunities for small groups of indigenous investors to those that provide opportunities for the entire population. In Africa, methods that broaden ownership have not been widely used. Despite the expressed desire by many governments to broaden ownership, only 44 management/employee buyouts, representing only 1 percent of transactions, have taken place. Other methods used include restitution and trusteeship arrangements. In some cases, notably in Ghana, Madagascar, and Zambia, and to a lesser degree in Burkina Faso, Tanzania, and Nigeria, some enterprises have reverted to private ownership through a process of restitution. Trustee arrangements have been used where governments want to demonstrate their commitment to transferring ownership to indigenous investors. The trusts are set up to warehouse shares temporarily until they are sold through public flotation. This was the mode used in Zambia. In Ghana and Tanzania, the governments have preferred to retain a block of shares for later sale to the public.

17. *Management and employee buyouts* are acquisitions by management or employees generally of the shares or principal assets of an enterprise. They can be through either a competitive process (with or without the management or employee team being given preferred terms) or a noncompetitive process. Although indigenous investors would clearly benefit from management and employee buyouts, there have been surprisingly few of these methods used in Africa. They have been tried only in Burkina Faso, Madagascar, Nigeria, and Zambia. In 1995, the Zambian government was eager to encourage employee participation and identified nearly thirty public enterprises that were considered suitable candidates for management and employee buyouts. However, only five management buyouts transactions were concluded. In several cases, unrealistic business plans relied too heavily on government or bank support; and inadequate allowance was made for much needed investment and working capital. In Nigeria, the only enterprise privatized through management buyouts is now in a financial and legal deadlock with major defaults on large bank loans.

18. *Employee share participation,* although probably on concessionary terms, is the same as a sale of shares. It may occur as part of a negotiated sale of shares to private investors or alongside a public flotation when a small block of shares is reserved for employees. Since management and employee buyouts tend to be feasible for small firms in which capital investment is minimal, governments often tend to encourage employee share participation in medium and large size companies alongside other new investors. In Benin,

such participation was mandated by the 1992 privatization Law. The law laid the principle for the creation in every denationalized firm of a savings fund that is to be used to allow employees to purchase shares in companies. However, the program has never been implemented. In Mozambique, 20 percent of the value of each privatized enterprise at the time of its sale was set aside pending the establishment of a stock ownership program for employees, who will be able to acquire shares on concessionary credit terms. In Cote d'Ivoire, in about eight privatization deals, up to 5 percent of shares have been reserved for employees. Although employee share participation can be politically attractive, its low incidence reflects the difficulties it poses for policy makers. Specifically, it can not be applied across the board; and thus, the employees in firms that do not offer employee share participation may feel that they are being treated unfairly. In addition, employee share participation extends deal negotiations and could reduce the overall price of shares.

19. *Directed group ownership* provides the opportunity for people who are functionally involved in a particular production sector with limited or no capital to participate in privatization. The scheme aims to broaden local participation by offering equity at discounted prices or on deferred terms. For example, in Uganda, directed group ownership has been successfully implemented in the Ugandan Tea Growers' Corporation. Tea growers are acquiring ownership through a scheme of registration and purchase at the time of sale of green tea to the factories. It was the first example in Africa of farmers being directly involved in privatization.

20. *Public flotation* provides shares to the general public through the stock market. It is sometimes referred to as an *initial public offering* or simply a *public offering*. On occasion, eligibility criteria are set in order to broaden ownership or to avoid a concentration of ownership. Although there is a degree of competition when subscribing for shares offered through a public flotation, applicants do not compete on price. Hence, a public flotation is categorized as a separate sale method. In West Africa, the planned regional stock exchange will extend this form of investment opportunity to citizens of all the UEMAO countries. However, the infancy of most capital markets in Africa represents a serious constraint on privatization. This has given added urgency to the need to improve banking systems, make venture capital available, and to establish markets for trading financial instruments. In this context, privatization is making an important contribution to private sector development.

21. *Financial intermediaries* can be used for privatization in the absence of stock markets or together with existing stock markets. Although many

African countries have been slow to use financial intermediaries for privatization, some countries have tried to do so. Zambia's principal method for broadening local participation is the Privatization Trust Fund (PTF) set up in 1994. The PTF is used as a vehicle for warehousing and then selling to the public minority shareholdings in certain major, newly privatized enterprises once the majority of shares have been sold by the Zambia Privatization Agency to core private investors. The PTF holds up to 30 percent of shares in companies the trustees consider to be worthwhile investments and later sells the issues to the public through public offerings.

2.5 Development of African stock markets

22. Privatization and stock market development are inextricably linked and mutually reinforcing. Although this close linkage was an explicit objective of many privatization programs in Africa, only Nigeria has mandated that all public enterprises be sold through the public offering of shares through its stock market. Interestingly, regional quotas have been applied to the public flotations in Nigeria in order to achieve an equitable geographic distribution of shares. Thirty-five out of the 49 public enterprises sold have been through public offerings. In Kenya, shares in the National Bank of Kenya were allocated on a regional basis to ensure equitable distribution. In Ghana, shares in Ashanti Goldfields were offered concurrently in Accra and London. Public flotations are the easiest way to reach as many people as possible. Where they have occurred they have given many Africans their first opportunity to become investors. The use of public flotations is, of course, restricted to those countries or regions that have stock exchanges.

23. Privatization has highlighted the need for stock market development in Africa. In so doing, it has provided the impetus for such development. Government sales of shares by public offerings have accounted for the increase in the number of quoted companies on existing stock exchanges. Although the amounts raised through privatization issues remain low, relative to total market capitalization, they are likely to increase. Almost 12 percent of the companies listed on the Nairobi Stock Exchange were privatization flotations.

24. Of all the methods of broadening ownership, public flotations through stock markets are the easiest and most efficient way of reaching the general public. However, some flotations involve companies in which there is already a core investor. Governments often want a core investor in larger enterprises before shares are floted to ensure that a sound management team and good corporate governance are in place. Another reason for having a core investor

is to improve operational performance prior to flotation. Without a core investor, corporate governance becomes a potential problem. Some enterprise managers can take advantage of a widely dispersed ownership. In Nigeria this risk was recognized, and, by promoting the establishment of shareholders' association, the privatization program sought both to encourage the active participation of small investors and safeguard their interests.

25. Given the stage of stock market development in Africa, most governments have adopted a policy of retaining an equity interest in some medium-sized businesses with the intention of floating shares at a later date, (differed public offers), or of transferring these shares to investment funds that will either resell the shares or float their own shares. Differed public offerings are planned in Kenya, Tanzania, and Uganda. Malawi has set up a unit trust investment fund for this purpose. Ghana is considering establishing an investment fund or a privatization trust. The problem is knowing when a government is serious about acting in a temporary trusteeship capacity and when such an arrangement is being used as a means by which the government will keep its foothold in commercial enterprises. To avoid any doubt, the transfer of government equity to an independent trust with a clear role and finite life is preferred. For example, Zambia established the Privatization Trust Fund for this purpose.

26. Many African countries have established new stock exchanges over the last decades. These include Botswana, Malawi, Swaziland, Zambia, Namibia, and Ghana. Other countries have worked on revitalizing existing, but largely inefficient exchanges, such as Kenya, Nigeria, and Zimbabwe; and some others are working to launch new markets. This has been possible by the assistance of the World Bank and IFC. The West African Economic and Monetary Union is also in the process of establishing a regional stock exchange in Abidjan which will serve its member countries – Benin, Burkina Faso, Cote d'Ivoire, Mali, Niger, Senegal, and Togo. The US Agency for International Development (USAID) has recently sponsored a study that explored the prospects of regionalization of stock markets in Southern Africa. The report examines the harmonization of securities laws, policies and operating standards to facilitate cross-border portfolio investment within the region and international portfolio investment into the region. To have any significant impact, however, a stock market requires a conducive economic, political, and regulatory environment for private investment.

27. The evolution of capital markets in Africa in recent years has been rather dramatic, as countries have sought not only to mobilize domestic resources but also to attract foreign direct investment. Accordingly, activity in a number of capital markets that had been dormant for years picked-up

significantly and a number of new markets have emerged. In a number of established stock exchanges, activity has been boosted by increased listings of companies; mostly made possible by privatization of state-owned enterprises. These changes took place within the context of economic liberalization programs and reflect in part efforts by many African governments to use stock markets as a means of privatization. In particular, stock markets are expected to play a major role in privatizing state-owned enterprises by facilitating public flotation of shares. The most prominent and successful example in this regard was the privatization of Ghana's Ashanti Goldfields, the biggest mining company in Sub-Saharan Africa, outside South Africa. The companies' shares were listed on the Accra Stock Exchange, the London Stock Exchange in 1994, and the New York Stock Exchange in 1996. The successful privatization of Kenya Airways in 1996 was another well-known example of public flotation through the stock market.

28. Moreover, many African countries recognized that stock markets offered an important means of attracting international capital flows. In the late 1980s and early 1990s, many African countries had began to reform their economies, and as part of their privatization and liberalization programs, opened up markets to foreign investors. When these efforts achieved some success, many markets – in particular Botswana, Ghana, Mauritius, Uganda, and post-apartheid South Africa, drew the attention of international investors. As interest in emerging markets heightened in the early 1990s, African stock markets received increased attention from international investment funds.

29. Stock markets in Africa are in different stages of development. The different experiences of the various stock exchanges reflects to a certain extent differences in policies towards capital markets as well as differences in macroeconomic developments, including exchange rate policies. The bursts in activity in certain markets coincided with major liberalization of these markets. These include, provision for access by foreign investors, improved macroeconomic stability, and liberalization of the financial sector. The creation of an environment that was supportive of capital market expansion and innovation played an important role in the expansion of activity that has taken place in a number of African markets. For example, in March 1994, the Ghanaian government sold half of its 55 percent share in Ashanti Goldfields, thereby quadrupling the number of shares traded on the Accra Stock Exchange.

30. One major concern by investors is the inadequate institutional system and operational procedures. Many stock exchanges are still in the process of developing, modernizing, or streamlining operational procedures. Therefore, trading and pricing mechanisms, clearing and settlement, and share

registration and custody practices remain outdated. A related problem is corruption. Activities such as insider trading and price manipulation severely undermine investors' interest. The Ghanaian market, for example, despite its high profile and strong image, suffers from the classic emerging markets problem of too few stocks, poor liquidity, slow settlements, antiquated systems, and lack of local investor interest.

31. The difficult investment environment in Africa has limited the growth and investors' interest in African stock markets. There is also some doubt whether stock markets can provide the expected economic benefits, particularly with regard to facilitating inflows of foreign capital and mobilizing capital domestically to finance development. Given the current state of economic development in most African countries, another important consideration is how many stock markets does Africa need? Many stock markets are either dormant or have only a few listed companies. For example, the stock exchange in Malawi has only one listing, and in Swaziland only four listings. Whether or not a stock market is appropriate for a country depends on the state of economic development, the size and depth of the private sector, the business culture, the general investment climate, and the nature of the financial sector. Therefore, it is clear that all countries do not need stock exchanges and the smaller ones are better off with listings on a regional stock exchange. However, small countries in Africa have come to regard a national stock market as a status symbol.

32. The fact remains that efficient stock markets are particularly desirable for African countries because they are a potential source of investor confidence in a country's commitment to a market-based economy and in the awareness of the globalization of the world economy. Attracting and sustaining capital flows requires that governments maintain policies to ensure political and economic stability. The down side is that, in exchange for these inflows and mobilizing domestic capital, government must contend with potential market volatility since domestic markets are no longer insulated form international capital markets developments. For this reason, many developing countries increasingly seek foreign direct investment (FDI) which is more stable and long-term. While FDI is more appropriate in many cases, African countries have difficulty attracting it for the same reasons that they are not able to attract portfolio investment.

33. African countries should encourage both international investors and indigenous investors by creating a conducive investment environment. At the same time, stock market development, be it national or regional; should be regarded as part of a long-term financial sector and economic development strategy, not a short-term source of finance.

2.6 Mobilization of investors

34. African governments' efforts to mobilize investors have been weak, and only four countries, Benin, Mozambique, Togo, and Zambia have used predominantly competitive methods of privatization. Guinea has received investor search assistance financed by donors for its first series of industrial privatizations. Madagascar called on the services of a merchant bank for privatization of a state-owned bank, and Uganda is using merchant banks to assist in the privatization of its telecommunications sector and a large bank. Ghana has included privatization in its general foreign investment promotion program, but many of the early deals were noncompetitive direct sales. Nigeria's marketing efforts were aimed at tapping small local investors proportionally among the different states, and public flotations were designed accordingly. Opportunities for attracting larger investors were therefore limited. In 1992 Kenya and Mozambique adopted policies that required international advertising and competitive bidding on a prequalification basis. Kenya failed to observe these policies, and Mozambique has privatized mostly very small enterprises, to which these policies did not apply. Burkina Faso intended to advertise internationally but was constrained by a lack of funds. Uganda and Zambia are now using the internet to advertise enterprises for sale. Only Benin is known to have regularly advertised its enterprises outside Africa.

35. The infancy of most capital markets has constrained privatization in Africa and investor mobilization by African authorities has remained very low. The need for capital market development in tandem with privatization has been recognized but, in terms of implementation, it has been weak. Only in Zambia was the opening of a sharehousing facility and a stock exchange planned and implemented alongside the privatization program. There are plans to open a regional stock market in Abidjan, but even when the market opens as planned, it will be much overdue for the countries in that region. Public flotations have mobilized investors in Ghana, Kenya, Nigeria, and Zambia. Except in Zambia, public flotations have generally been combined not with the entry of core private investors, but rather with a retention of government shares. Only Ghana and Kenya floated shares outside the country.

36. The major single investors in privatized Africa are foreign. In some countries, including Ghana, Kenya, and Zambia, sales to existing foreign shareholders with preemptive rights have been among some of the most important transactions. Attracting new investors has been difficult. Many countries find that foreign investors tend to be those who were already present before privatization began. Nonetheless, the picture is changing as the larger

enterprises come on stream. In Ghana, the recent privatizations in the banking and telecommunications sectors have introduced new foreign as well as indigenous investors.

37. Although the difficult investment environment may at least partly account for the problem of attracting new investors, it does not explain why so few agencies have used investor search facilities, and why only one agency in Zambia maintains dedicated publicity and marketing activities. Except for the occasional use of merchant banks and the International Finance Corporation, which has advised on transactions in several African countries, the search for qualified investors has been restricted to a few advertisements, often only in the local press. Privatization agencies often neglect to establish the profile of investors likely to be attracted by an enterprise and capable of meeting its needs. Part of the problem lies in the lack of experience in private investment markets. That lack of experience has not been compensated for by external expertise because privatization agencies do not have sufficient funds to hire outside experts. Apparent weak efforts to mobilize investors may also reflect the inherent conflict between the aim of maximizing sale prices and the objective of broadening ownership among the population in which the majority have no savings. Agencies may have shied away from publicly generating investor interest because what makes good for attracting investors, particularly foreign investors, may not be politically appealing to the indigenous majority. But if privatization is to attract investment and attract optimum deals, program design and preparation must allow for more concerted efforts to make both local and foreign investors aware of the opportunities.

2.7 Country-specific efforts to broaden local participation

Burkina Faso *– Consortium of local and foreign investors*

38. When a pharmaceutical importing company was put up for sale in Burkina Faso, the highest bidder was a foreign investor. At the bid selection phase, the foreign investor was asked to form a consortium with the association of Burkinabe pharmacists that had submitted a lower bid. Although this condition led to long negotiations, a satisfactory conclusion was reached, with both the foreign investor and local investors becoming owners of the enterprise.

Cape Verde *– A participatory approach*

39. A participatory approach to privatization was used by the government of Cape Verde. The government successfully mobilized public support for reforming the public enterprise sector and implementing a privatization program. To do so, it developed a well-conceived, aggressive, and sustained television and radio information campaign. The campaign highlighted opportunities for higher growth led by private sector reform. During the implementation of the privatization program, public anxiety rose regarding the impact of the program on an already difficult unemployment situation. In response, the government with the support of the World Bank, organized a series of orientation visits to countries such as Mauritius, which had gone through similar private sector reform and liberalization processes. Participation in these programs was targeted at opinion leaders, local elected officials, local business representatives, and key civil servants. These visits proved instrumental in convincing a large number of the population of the potential of the reforms, and in rallying support for the necessary steps to complete the reforms. Finally, the privatization agency itself tried at every step to ensure that the needed liquidations, restructuring, and privatizations have been carried out with a minimum of labor unrest and disruption. This has been achieved through its participatory approach to the process, in particular, its constant efforts to involve the people most affected, workers and managers, in the discussion of privatization options. Moreover, the privatization agency's creativity in designing socially acceptable solutions, mainly through the use of management/employee buyouts; and its proactive provision of support to the newly privatized enterprises made the reform process mutually acceptable.

Kenya *– Politically acceptable ownership*

40. The government of Kenya sought a foreign strategic partner to participate in the privatization of Kenya Airways after intensive restructuring of its national airline. The government wished to achieve a politically acceptable ownership distribution, balancing the benefits of a foreign partner, against the partner's desire, to maintain local majority ownership. The debt-saddled enterprise was overhauled in the early 1990's when the government replaced the entire board and gave it a mandate to prepare the airline for privatization. The operations, management and labor force were restructured over a period of three years, and a divestiture policy that would cement these changes through privatization was identified. Finally, in January 1996, a 26 percent stake was sold to the Dutch Royal Airline, KLM. In addition to the 26

percent stake taken by KLM, shares were also listed on the London and Nairobi stock exchanges, with both offerings oversubscribed. Kenyan institutions and individuals acquired 34 percent of the shares and international investors 14 percent. Airline employees enrolled in a special program to purchase 3 percent, and the government of Kenya retained 23 percent. As many as 110,000 different shareholders participated in the domestic offering.

41. The deal with KLM included several features that appealed to the Kenyan authorities. First, the price paid by KLM reflected a value for Kenya Airways that was three times its book value. Second, the proceeds went directly to the Treasury. Third, KLM did not in the end require a management contract or unusual minority privileges, which means Kenyan interests will control the company, a feature expected to help attract Kenyan investors.

Uganda *– Directed group ownership*

42. Having considered the options of privatizing four tea factories under the Uganda Tea Growers' Corporation (UTGC), the government of Uganda decided to adopt a proposal that would involve the farmers themselves. The first hurdle to overcome was the value of the factories, each of which was valued at about $3.5 million, a price considered too high for the farmers to afford. It was therefore decided to base the sale price on the value of the factory shell by omitting land and other values. This decreased the value of each factory to half a million, and donors agreed to pay off the loans attached to all of the factories. In order to get the privatization process started, a neutral bank, the Development Finance Company of Uganda (DFCU) was appointed to act as a trustee.

43. To date, tea growers are acquiring ownership through a scheme of registration and purchase at the time of sale of green tea to the factories. Each farmer initially pays 5,000 Ugandan shillings to participate. Share allocations are based on the minimum subscription and thereafter on production, up to a limit. Each tea factory has a board of directors comprising of six elected shareholders, representing farmers and the institutional investor. Encouraged by the success to date, the government of Uganda is considering adopting the same directed group ownership privatization approach for the dairy sector. Farmers are pleased with the scheme and feel they are involved in the privatization process.

Zambia – *Privatization trust fund*

44. Zambia's principal mechanism for broadening ownership is the Privatization Trust Fund (PTF). The PTF was set up 1994 as a vehicle for warehousing and then selling to the public minority shareholdings in certain major, newly privatized enterprises once the majority of shares have been sold by the Zambia Privatization Agency (ZPA) to core private investors.

45. The Lusaka Stock Exchange (LSE) began operations in January 1994 and formally opened for business on February 1994. The LSE has been constituted as a private nonprofit company owned by the members of the exchange, with each member having a single share. The LSE has a small full-time staff led by a general manager. The Securities Act, enacted in December 1993, established the Securities and Exchange Commission to regulate all participants in the stock market with the prime purpose of protecting investors.

46. The PTF's objectives are to enable the widest number of Zambian citizens to participate in the privatization process, to protect the value of the minority shareholdings until they are sold, and to ensure transparency. The PTF gives priority to individual Zambian investors who wish to acquire a small number of shares. If, however, less than favorable market conditions prevail, it will sell shares to financial institutions who are investing on behalf of Zambian citizens. To avoid flooding the market with public offering, the PTF coordinates its efforts with ZPA, the LSE, and institutional investors. A board of trustees, four of whom are drawn from the private sector, oversees the operations and financial position of the PTF. The PTF is managed on a daily basis by a management company, which is remunerated by a fixed monthly fee plus a performance fee determined on the basis of the company's ability to sell shares. The PTF was established for a period of only five years. If at the end of the period all shares transferred to the PTF have been sold, it will be liquidated. If some shares remain unsold, the PTF will convert into a unit trust. The ZPA has identified 14 companies as prospective candidates for eventual government shares to be transferred to the PTF. By the end of 1996, the ZPA had transferred the residual government minority shareholdings in four campanies. Twenty-seven percent of the shares in Chilanga Cement Company, were offered and fully subscribed in May 1995. Seven percent of the shares in Zambia Sugar Plc. were offered for sale in August 1996, leaving a further 23 percent in that company to be sold by the PTF.

Zimbabwe *– Unit trust*

47. Zimbabwe changed its securities and foreign investment regime in April 1993, leading to a flood of foreign portfolio investment during the last quarter of that year. Beginning in 1993, a small fund manager began to set up a series of unit trusts. While these were small, they provided a basis for the development of proper unit trusts in acceptable legal framework. With the institution of this vehicle, household participation is expected to rise and the government can use this vehicle to make privatization more politically acceptable. Now, small household investors can participate in the sell-off of government assets.

III. The Road Ahead

3.1 Improving the process

48. Over a decade of experience across Africa in privatization has provided clear lessons on how to improve the process. These lessons suggest changes to improve the process and its outcome, and the changes require a great deal of commitment. At the present, most governments declare their commitment to privatization, but they have to do more to demonstrate it. Commitment is essential, but so is consensus.

(a) Securing consensus

49. Great attention should be paid to securing consensus by African countries embarking on privatization. Evidence suggests that privatization in African countries has mostly been adopted as a matter of economic necessity, with strong pressure from international organizations and donors. Senior persons in government may have been convinced of the benefits of privatization, but there has not always been a consensus throughout government and certainly not among the general public. Although some efforts have been made to secure consensus, much more could have been done to convince stakeholders of the benefits, desirability and feasibility of privatization.

50. *A participatory approach to privatization by providing public information and encouraging debate* is the best way to secure consensus. For example, the government of Cape Verde has successfully mobilized general public and local government support for reforming public enterprises and implementing a privatization program. To do so, it developed a well-conceived, aggressive, and sustained television and radio information campaign. The campaign highlighted opportunities for higher growth led by the private sector. This has been achieved through its participatory approach to the process of privatization; in particular its constant efforts to involve the people most affected in the discussion of privatization.

51. Securing consensus involves presenting facts and arguments to convince a majority of the population. Thus, Governments must provide and encourage debate. People need to understand why privatization is important, what benefits it can bring to them, and the context in which indigenous investors can participate. An early starting point should be to gather and disseminate information about the public enterprises sector, the economy

generally, and the possible options and tradeoffs. This calls for effective use of the media through carefully designed advertising and public debate. Representatives of all stakeholders should be encouraged and permitted to participate in discussions on privatization, objectives, options, priorities and the alternatives. Informed and constructive debate requires full disclosure of information. Disclosure can be difficult for a government when there are major gaps in data and poor results, reflecting poor decisions and management in the past. Disclosure also requires more be done to clarify objectives and, later, to report progress towards achieving those objectives.

52. Ownership and employment are usually at the center of public concern. These issues need to be debated openly so that the tradeoffs become known and better understood. Many public enterprise sector employees can be expected to feel threatened by the prospect of privatization. An important way in which to alleviate their concerns is to inform them of the experiences of successful privatization cases, including the potential for increased local participation. In this respect, privatization methods that broaden local participation, such as employee share participation and directed group ownership, should be highly encouraged.

53. Occasionally, opposition to the process of privatization will arise as opportunists seek political gain. Although in some cases they may be advocating a failed ideology, the principal reasons for opposition are usually ignorance and misunderstanding. In some African countries they are becoming more outspoken in their opposition. After all, it is easier for doubters to raise concerns about an untried process than to convince the public of a new concept that is remote from their experiences. In some countries the large majority of the population may be ambivalent about privatization. If that is the case, it is incumbent on a government committed to the process to present the case clearly and unequivocally through a well-managed public information and constructive debate. Information needs to be communicated in ways audiences will understand, and this demands a carefully designed and executed information campaign. Particularly, careful handling is needed for certain issues, including the need for nonviable businesses to be liquidated, and the potential effects on labor, the position and rights of existing shareholders with preemptive rights, the need to attract foreign investors and ways in which indigenous investors can benefit.

54. *Governments should deal with labor issues upfront*. Governments and their agencies have tended to avoid open discussion on the effects of privatization on labor. Difficulties over the level of payment of employee severance pay, end-of- service benefits and the absence of a social safety-net have caused governments to be extremely silent. The longer the issues are not

addressed, the greater the concern of workers, and the more difficult it is to build consensus. Labor representatives should be party to developing mechanisms to deal with these issues, and be shown the real opportunities for sustained employment through the introduction of new capital into businesses.

55. There is no doubt that privatization will bring about improvements in efficiency, but there is a widespread concern that it will have a negative effect on employment. African governments have taken rather different policy approaches to employment in privatization, reflecting the political capacity to absorb the consequences of retrenchment. In Zambia, where the government depends on an urban electorate, liberalization and privatization have been controversial. Accordingly, the government required the privatization agency to try to negotiate employment-etention conditions in privatization transactions and also legislated improved employee end-of-service benefits. In Ghana, where the government depends more on a rural electorate that has benefited from liberalization of agricultural markets, the government has set few employment-related conditions on privatization. In Africa, layoffs have not occurred in some enterprises because bidders were required to maintain existing employment levels or, at the very least, were encouraged to do so. In Mozambique, one of the criteria for evaluating bids is the bidder's commitment to maintaining the labor force at the existing level, although, in practice, the commitment has not always been kept. In Burkina Faso, employment conditions are included in the sales contracts, and buyers are required to maintain employment at particular levels. Both Benin and Zambia have used employment guarantees. These guarantees have not always been easy to enforce. In Zambia, several companies retrenched workers despite the guarantee. By contrast, companies in Benin wanting to downsize their workforce have been prevented from doing so by a five-year no layoff clause as standard in privatization contracts.

(b) Ensuring transparency

56. Transparency is essential for building and ensuring consensus. There should be a clear policy on how proceeds will be managed and utilized. As more stakeholders enter the debate and greater press coverage is given to privatization, greater transparency will be demanded. It is preferable that transparency be achieved by privatization agencies according to published procedures and by issuing regular public reports rather than as a reaction to criticism. One area where transparency is very absent is the publication of financial accounts of privatization programs which disclose, among other things, the use of privatization proceeds. To date, only the privatization agency in Tanzania has published financial accounts. Governments risk

adverse speculation and publicity if the public is not informed about the use of privatization proceeds. Progress reports on privatization should include a section setting out how much of the proceeds have been applied to meet transaction costs, program management, end- of-service benefits, general debt-servicing by government, and other specific government expenditure items.

(c) Investing more in design and preparation

57. Governments should invest more resources and time in design and preparation of privatization programs. This is an important lesson that countries which do not yet have a program in place can learn from other countries' experience. This means investing more in the critical early stages of the privatization program where, the level of resources made available is an early indication of government and donor commitment. Access to information about the wealth of experience around the world should be available to all privatization agencies. In this regard, the World Bank is now playing an increasingly important role in providing best practice guidelines.

58. Some key areas in which more effort in design and preparation will contribute to a successful privatization program in general and to broadening local ownership in particular, include: determining objectives and priorities at the program and enterprise levels; examining and designing strategies for identifying and attracting core investors including indigenous investors; and involving the private sector in the privatization process. Policy issues affecting sectors and individual enterprises need to be identified as early as possible and efforts must be made to examine options, make decisions, and draw up detailed policies which enable the implementation agency to move forward quickly and consistently. Regarding ownership, although there will be a general policy on ownership, where a number of enterprises with similar characteristics can be aggregated, there will be need to review and decide on the most appropriate ownership structure. Moreover, since broadening local ownership is one of the major objectives of African countries' privatization programs, employee share participation should be given an appropriate consideration in the design of ownership structure.

(d) Ensuring appropriate institutional building blocks

59. The three most important building blocks of privatization programs are the enactment of appropriate legislation; the granting of sufficient authority, independence, and resources to the privatization agency; and the removal of obstructive influences of holding companies and ministries. Delays,

uncertainty and poor publicity for privatization send the wrong message to investors. Therefore, it is important to put the building blocks for privatization in place before launching a program.

60. *Enacting appropriate legislation and addressing the need for more competition* will facilitate privatization. Appropriate legislation allows deals to be approved and finalized more quickly, and that is very crucial to attracting potential investors locally and abroad. In addition, given the commitment by government to private sector development and privatization, addressing the need for competition should be given high priority.

61. Except for Ghana, African countries have not cited encouragement of competition as a specific objective of privatization, although it may be inferred from the objectives of private sector development and increased economic efficiency. This is a crucial point because, in most cases competition is of a major importance. In Tanzania and Zambia, for example, competition, facilitated by the liberalization of crop marketing and road transport services, has brought about major benefits to growers and consumers, before privatizing public enterprises in those sectors. Ghana also stands out as the first African country to license a second general telecommunications provider, and it is doing so at the same time as it is introducing a core investor into existing utility. The government's policy is to stimulate investment and improvements in telecommunication services by introducing competition as early as possible. This is in contrast to other countries that prefer to privatize but continue with a telecommunications monopoly.

62. *Empowering the privatization agency with the necessary power, independence, and resources* is essential. Experiences in Africa indicate that the best arrangement is to establish a central privatization agency with legal status and sufficient authority to initiate, negotiate, and conclude transactions. Establishment of such an agency does not mean that one agency must handle every transaction. Some privatization can be delegated. However, it does mean that one agency should oversee the programme and report to the main legislative body and the public. The agency should, to the extent possible, be independent of the government. To be truly effective, the agency must have access to adequate resources and approach privatization in a commercial manner. This means being able to avail itself of the best advice, to use the media effectively, and to contract out the work on individual privatization transactions to experienced professionals. A person regarded by the general public as having integrity, political clout, and commercial insights should head the agency.

63. *Eliminating the influences of vested institutional interests* facilitates the process of privatization. Privatization can be accelerated if steps are taken to eliminate the influence of institutions with vested interests. In particular, state-owned holding companies and associated ministries, which do not want to lose the privileges afforded by the exercise of ownership rights in public enterprises, should gradually be eliminated. When a sufficiently competitive environment has been established, holding companies themselves can be privatized. This would transfer their entire investment portfolio to the private sector.

64. Finally, in all the above major procedures in improving the process of privatization, namely, securing consensus, ensuring transparency, investing more on design and preparation and ensuring appropriate institutional blocks, the objective of broadening local participation reinforces the whole privatization process. ***Specifically, broadening local participation in privatization secures consensus of the general public, helps to depoliticize and speed up the process, indicates a strong commitment to transparency and sends an encouraging signal to foreign investors***. Therefore, more steps should be taken to broaden ownership, using all the methods available, with preference given to those methods that reach out to more people. Capital market development should take place in tandem with privatization. To attract indigenous private entrepreneurs, venture capital funds need to be established and made accessible.

3.2 Replicating 'best practices' of directed group ownership

65. Given the infancy of stock markets in Africa, an alternative medium-term solution is of a critical path to broaden the participation of indigenous investors in the privatization of public assets. Methods like directed group ownership can be implemented for broadening local ownership in the absence of stock markets or with existing stock markets. The choice of directed group ownership as replicable 'best practices' is based on the following: the method has been extremely effective for broadening local participation for the intended privatized state-owned enterprises, e.g. Uganda and Burkina Faso; the type and nature of the state-owned enterprises privatized in these countries are very typical across the board in Africa; and, most importantly, the ease in which the methods were implemented makes them a major candidate for replicable 'best practices'.

66. Directed group ownership aims to broaden ownership by offering equity at discounted prices or on deferred terms to people involved in a particular sector. It provides the opportunity for indigenous investors with long-term or permanent interest in a sector – but with limited or no capital – to participate in privatization.

67. This study envisages and recommends two workable and possible scenarios in which a directed group ownership scheme could facilitate to broaden local participation in privatization of public assets. In the following scenarios, it is assumed that African farmers are the indigenous investors who supply their agricultural outputs to factories (state owned enterprises) that are subject for privatization.

Scenario 1 – *Farmers with large output supply*

68. As farmers sell their agricultural output to a factory to be privatized, a certain portion of their supply (e.g. 20 percent) will be registered to be converted to some share of the privatized factory on the spot.

Scenario 2 – *Farmers with small output supply*

69. For those small farmers who cannot afford even the minimum share value, they should be able to buy a token mini-share (some fraction of the minimum real share) from a 'farmers share association'. The major responsibilities and functions of the 'farmers share association' would be:

- to collect the token mini-shares and put them in a sizable 'bundle' and use the 'bundle' of token mini-shares to buy real shares from the privatized enterprises for the farmers;
- to divide up and distribute the real shares to the farmers at the time of liquidation;
- to keep all accounts and proceeds for the farmers and disseminate information;
- to act as intermediary between the enterprise to be privatized and the farmers to facilitate local participation; and,
- all the burden of share administration lies on the 'farmers share association'.

70. In the above scenarios, the government must play an active role in warehousing a certain percentage of shares for indigenous investors to be used for directed group ownership. When deferred payments and bank

guarantees are possible, it makes it even easier for farmers or other indigenous investors to participate in privatization through directed group ownership.

3.3 Activating mass privatization through voucher scheme

71. All the methods that have been tried in African countries to broaden local participation in privatization, such as, management/employee buyouts, employee share participation and directed group ownership have certainly planted the seed for some participation by indigenous investors. On a case-by-case basis, some of the efforts by African countries to broaden ownership using these methods have been highly successful for the intended enterprises. However, the problem with all these methods for broadening ownership is that they directly reach only the minority of people who have some savings or are employees in enterprises in which equity participation is available. Of course, some people benefit from improved utility and transport services, but still a significant proportion of the population does not directly gain from or observe any indirect benefits from privatization. Given the importance attached to broadening ownership by African governments, it is somewhat surprising that more efforts have not been put into developing a mass privatization scheme that could be widely used in Africa.

72. The design and implementation of mass privatization through voucher scheme would be undoubtedly difficult, but, given a strong commitment, it can be achieved at least in the long-term. Although communications are poor, voter registration difficult, and illiteracy widespread, many African countries already have some active private sectors. Therefore, the reluctance to use at least some form of voucher-based scheme is surprising. In addition to privatization, improving communications and voter registration procedures that would be needed for a voucher-based scheme would be extremely beneficial to the economy and the process of democratization.

73. There are few reasons that account for the reluctance to examine mass privatization further. First, financial and technical resources are scarce. The considerable resources required for planning and implementing a mass voucher-based scheme are beyond what most African countries can undertake. As it is, government and donor commitments to privatization are much lower in Africa than elsewhere in the developing world, and programmes for the development of mass privatization have not been sponsored in Africa. Second, mass privatization would not only be costly; it would raise no capital. Third, unless all the utilities were included, the market value of the privatized firms might be too low. When companies with

shareholders with preemptive rights are excluded, the earnings potential of the remaining public enterprises is often very low. The cost of mass privatization schemes thus might outweigh any benefits assigned to the public. Fourth, in some countries it is possible that potential ethnic and political frictions have added to the reluctance to implement a voucher-based scheme for privatization. Despite these drawbacks, African governments may have to consider some form of voucher scheme if the general public is to be convinced that privatization will benefit them.

74. Given the above drawbacks, as an alternative to voucher schemes, more efforts should be directed toward identifying targeted groups to whom share discounts or credit could be offered. Without a major attempt to broaden ownership on a larger scale than has been achieved so far, privatization will continue to be perceived as benefiting mostly foreigners.

3. 4 Creating a conducive investment climate

75. Public flotation through the stock market is the easiest way to reach as many people as possible. Their use is, of course restricted to those countries that have stock exchanges. The positive impact stock markets will have on any individual African country is dependant on the evolution of an attracting investment climate. Progress on reforms in Africa, however, has been limited to only a few countries and there is no strong evidence that the investment climate has improved. Both local and international investors view African countries as having very low conducive investment climate. Creating a conducive investment climate requires significant institutional reforms that guarantee property rights, effective legal systems to ensure the rule of law, and bureaucracies that foster rather than obstruct the private sector and investment. These structural reforms are important and relatively straightforward. However, the more difficult impediment to both domestic and foreign investment is the harsh and complex regulatory environment, bureaucratic red tape, corruption, poor infrastructure, unproductive labor force, and hostility toward both the private sector and foreigners.

76. Problems relating to political, economic, regulatory, and institutional reforms are not unique to African countries; they apply equally to many of the newly emerging markets. But African countries, with the lowest savings rate in the world, need both foreign and domestic investment more than any other developing region. African governments can overcome the region’s poor image and low ranking among developing countries only by establishing policies to provide attractive returns for investors, draw capital, and promoting the private sector. Most African countries have embarked on

reforms only as a result of arm-twisting by major international organizations and other donors. Many African countries, however, have failed to take the steps toward creating attractive investment climate and building investor confidence. Some actions remain largely guided more by individual political interest and personal financial enrichment than the national interest. Thus, liberalization and privatization programmes, whose success ultimately erodes politicians' power and control over the economy in general and the public sector in particular, are implemented only reluctantly. **Therefore, acquiring credibility with both foreign and indigenous investors is key to promoting investment in privatization.**

77. As experiences in other emerging markets demonstrate, even in countries dedicated to reforms, efforts to create attractive investment climate take a long time to bear fruit. In Africa, these problems remain especially difficult. For example, even relatively stable and reforming countries must bear the negative consequences of an upheaval in any other country because it reinforces the perception that such negative effects could take place in any other African country. Nevertheless, there appears to be the recognition that pan-African efforts could improve the political and economic environment. **Continent-wide efforts are necessary to ensure stability and to improve the investment climate.**

78. Despite the real danger that Africa will become even more marginalized in the global economy, there is not a sufficient sense of urgency in Africa to address and improve this global perception. Perhaps the globalization of finance, trade, and telecommunications technology will force African governments to realize sooner rather than later that they must make genuine efforts to foster political and economic stability and strengthen the institutions involved to create a conducive investment climate. A healthy investment climate together with a continued assistance of donors can set in motion a rapid transformation of African economies into a very attractive investment environment.

Conclusion and recommendations

79. Broadening local participation has been cited as one of the major objectives of privatization programmes by African governments. However, with few exceptions, only minor efforts have been made in this direction. Much more needs to be done to reach out the majority of the population in every country that has little or no savings, and is therefore unable to participate in privatization under most of the methods currently employed.

4.1 Stock markets – as a long-term solution

80. In general, public flotations through the stock market are the easiest way to reach as many people as possible. Therefore, stock market development and improvement should take place in tandem with privatization. For stock markets to have a significant positive impact in broadening local participation in privatization, the following major tasks must be undertaken:

- to attract indigenous investors through public offerings, venture capital funds needs to be established and the development and improvement of either a national or a regional stock market is essential;
- it is crucial to convince small indigenous investors that they should not expect to buy shares and then make quick financial gains through early sale. The culture of long-term investment must be encouraged and developed;
- stock market development should be regarded as part of a long-term financial sector and economic development strategy, not a short-term source of finance; and,
- African governments should encourage both domestic and foreign investors by creating continent-wide conducive investment climate. Only then will stock market and other financial institutions play a significant role in the mobilization of both domestic and foreign resources.

4. 2 Directed group ownership – as a medium-term solution

81. Given the infancy of stock markets in Africa, an alternative medium-term solution is of a critical path to broaden the participation of indigenous investors in the privatization of public assets. Methods like directed group ownership can be implemented for broadening local ownership in the absence of stock markets or with existing stock markets. The choice of directed group ownership as replicable 'best practices' is based on the following: the method has been extremely effective for broadening local participation for the intended privatized state-owned enterprises, e.g. Uganda and Burkina Faso; the type and nature of the state-owned enterprises privatized in these countries are very typical across the board in Africa; and, most importantly, the ease in which the methods were implemented makes them a major candidate for replicable 'best practices'.

82. To sum it up, because of the inescapable fact that privatization and stock market development are inextricably linked and mutually reinforcing, the development of stock markets and the use of public flotations in Africa are highly recommended as a long- term solution to broaden ownership of indigenous investors. In addition, and with equal importance, it is also recommended that the method of directed group ownership as 'best practice' should be implemented as a medium-term solution concurrently with stock market development for an optimal path to broaden local participation in privatization of public assets.

Tables

Table 1: Summary of Divestiture Transactions and Sales Values in sub-Saharan Africa, as of End 1996

Country	Prior to 1990	'90	'91	'92	'93	'94	'95	'96	Year not known	Total no. trans-actions	Total sale value (US$m)
Angola	-	-	-	-	-	-	-	56	275	331	25.1
Benin	17	3	8	3	5	3	5	-	2	46	63.5
Botswana								-	1	1	-
Burkina Faso			2	1	5	5	3	-		16	9.6
Burundi	4		2	12	7	1	-	13		39	10.8
Cameroon			8			5	3	23		39	-
Cape Verde					1	10	10	9		30	24.1
CAR	17	4	5					-		26	-
Chad						12	12	10		34	-
Comoros					4	-	-	-		4	0.2
Congo, D. Rep.	16						3	3		22	-
Congo, Rep. of				2			44	14		60	-
Cote d'Ivoire		1	3	4	3	8	18	9		46	123.1
Djibouti								-	1	1	-
Eq. Guinea					2	-	-	-	1	3	0.2
Ethiopia							9	-		9	31.3
Gabon								25		25	-
Gambia, The	8	7	4	5	3	3		-		30	9.9
Ghana	4	33	13	14	9	83	24	12		191	417.3
Guinea	76	8	2	6	16	2	4	-		114	8.9
Guinea-Bissau	2	3	3	7	1	3	11	-		30	1.3
Kenya				27	21	16	66	22		152	184.6
Lesotho							8	-		8	-
Madaga-scar	14	11	10	21	1	3	24	-		84	18.8
Malawi	35	-	-	-	-	-	-	9		44	55.9

Mali	2	4	18	30	-	-	-	-		54	31.8
Mauri-tania	13	1	-	15	-	-	3		15	47	1.2
Mozam-bique	65	40	53	62	42	136	112	38		548	179.7
Namibia							-	-	1	1	-
Niger	20	4	2	1	1	1	2	-		31	3.5
Nigeria	15	36	8	14	8			-		81	206.9
Sao Tome & Prin.		5		2	1		1			9	-
Senegal	12	7	17		-	-	-	9	3	48	65.0
Seychel-les							-	-	1	1	-
Sierra Leone					6	1	1	-	1	9	-
South Africa	2		1					1		4	761.7
Sudan				12	17	3	-	-		32	-
Swazi-land								-			-
Tanza-nia				13	33	16	27	34		123	125.5
Togo	12	5	3	2		3	1	19		45	35.9
Uganda			1	3	3	29	25	15		76	136.9
Zambia					6	20	58	107		191	146.3
Zimba-bwe						4				4	25.0
Total	334	171	163	256	195	367	474	428	301	2,689	2,704.1

- Not available

Source: World Bank data.

Table 2: The Top 20 Transactions Accounted for More Than a Third of Total Value

Country	Name of enterprise	Date of sale	Government ownership (per cent)		Total sales value (US$m)
			Before sale	After sale	
Ghana	Ashanti Goldfield Corporation	1994	55	30	316
South Africa	Radio Stations	1996	100	0	129
Kenya	Kenya Airways	1996	100	20	74
Tanzania	Tanzania Cigarette Company	1995	100	0	55
Senegal	SOCOCIM	1991	97	0	39
Zambia	Zambia Sugar Plc.	1995	100	0	37
Nigeria	Festac 77 Hotel Plc., Lagos	1992	100	0	31
Benin	La Beninoise	1992	100	0	28
Uganda	Nile Hotel Complex	1995	100	41	27
Nigeria	Tourist Co. of Nigeria	1992	100	0	25
Tanzania	Tanzania Breweries	1992	50	50	23
Cote d'Ivoire	SOGB	1995	95	35	22
Uganda	Hima Cement Factory	1994	100	0	21
Mozambique	Cementos des Mozambique	1994	100	49	20
Cape Verde	Cabo Verde Telecom	1995	100	60	20
Kenya	National Bank of Kenya	1996	63	23	18
Ethiopia	Coca Cola Bottling Plant	1995	100	0	17
Nigeria	Nigeria Hotels Plc.	1992	47	0	16
Benin	Societe Nationale des Ciments	1991	100	0	16
Ghana	Achimoto Brewery Co. Ltd.	1991	100	0	16
Total					950

Note: Excludes transactions prior to 1990.
Source: World Bank data.

Table 3: Numbers of Transactions Are Not Correlated with Values of Transactions

Country	Number of transactions 1988-1996	Total sales value (US$m)	Average sales value (US$m)
Ghana	191	417.3	2.2
Nigeria	81	206.9	2.6
Mozambique	548	179.7	0.3
Zambia	191	146.3	0.8
Uganda	76	136.9	1.8
Benin	46	63.5	1.4
Kenya	152	184.6	1.2
Togo	45	35.9	0.8
Madagascar	84	18.8	0.2
Burkina Faso	16	9.6	0.6
Total of major privatizors	1,430	1,399.5	1.0
Other sub-Saharan Africa	1,259	1,304.6	1.0
Total sub-Saharan Africa	2,689	2,704.1	1.0

Source: World Bank data.

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