FINDING BALANCE 2014

BENCHMARKING THE PERFORMANCE OF STATE-OWNED ENTERPRISES IN ISLAND COUNTRIES

ASIAN DEVELOPMENT BANK

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ADB

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FOREWORD

Pacific island countries recognize the importance of vibrant private sectors to drive economic growth. Since 2002, they have introduced important policy reforms to improve the environment for the private sector, and these are beginning to translate into increased formal business creation and investment. State-owned enterprises (SOEs) continue to constrain Pacific economies—and other island economies outside the Pacific—by absorbing large amounts of scarce capital, low productivity, and often limited service coverage. Reforming the SOE sector is vital for private sector development, as it will create opportunities for private investment, reduce the costs of doing business, and improve basic service delivery.

This is the fourth comparative study of SOE performance in the Pacific undertaken by the Asian Development Bank (ADB), and the first to include island countries from the Atlantic Ocean (Republic of Cabo Verde, or “Cabo Verde”), the Caribbean (Jamaica), and the Indian Ocean (Mauritius). This expansion of the study was specifically requested by the Pacific island countries to provide a more global benchmark for their SOE sectors. The study assesses SOEs’ impact on the participating countries’ economies, and identifies key performance drivers and reform strategies to guide future policy action. A key theme is finding the balance between the roles of the public and private sectors.

The study reflects ADB’s ongoing commitment to increasing south-south cooperation on economic development issues and thought leadership on SOE reforms. The nine participating countries (Cabo Verde, Fiji, Jamaica, Republic of the Marshall Islands (or, “the Marshall Islands”), Mauritius, Papua New Guinea, Samoa, Solomon Islands, and Tonga) were selected for their comparability and SOE reform experience. We commend their participation as demonstrating their governments’ willingness to identify and address the core issues within their SOE sectors. This transparency is an essential precursor to successful reform.

SOE reform requires strong political commitment, and this study demonstrates that this is extremely difficult to sustain over prolonged periods. Involving the private sector through public–private partnerships and privatization is a more effective way to sustain improved SOE performance and service delivery, respectively. Competition for investment capital means that the private sector will always have stronger performance incentives than the public sector. These incentives should be harnessed to support public service delivery. Governments engaging in SOE reform are therefore asking the key questions: (i) what is the appropriate role of the state in the economy; (ii) does the government need to own and manage state assets to deliver public services; and (iii) can these services be contracted to private sector providers.

ADB has been working with its developing member countries on SOE reforms for many years. Lessons from this experience are increasingly shared among countries and between regions. In the Pacific, the Finding Balance SOE benchmarking studies are now recognized as both an important SOE performance scorecard and a valuable knowledge repository about effective reform strategies.

I sincerely thank the governments of all participating countries for their extensive inputs, without which this study would not have been possible. I also wish to thank the authors (Laure Darcy and Christopher Russell) and financial analyst (Minh Vu) for their efforts; and the Government of Australia and the New Zealand Government, which provided cofinancing under the Pacific Private Sector Development Initiative.

I am confident that the study will provide thought-provoking insights and stimulate useful discussions, toward further progress in SOE reforms in the Pacific and other regions facing similar challenges.

Xianbin Yao
Director General, Pacific Department
Asian Development Bank

ABBREVIATIONS

ADB	Asian Development Bank
ADP	IPE–Aguas de Portugal
AFL	Airports Fiji Limited
AJ	Air Jamaica
AML	Air Mauritius Limited
AMU	Asset Management Unit
ASA	Empresa Nacional de Aeroportos e Segurança Aérea (National Airports and Safety Company)
CAL	Caribbean Airlines Limited
CEO	chief executive officer
CSO	community service obligation
DSPE	Direcção de Serviço das Participadas do Estado (Directorate of Service of the State Shareholdings)
ELECTRA	Empresa de Electricidade e Água (Electricity and Water Company)
ENAPOR	Empresa Nacional de Administração dos Portos (National Ports Administration Company)
FEA	Fiji Electricity Authority
GCC	government commercial company
GDP	gross domestic product
GoJ	Government of Jamaica
IPBC	Independent Public Business Corporation
MEC	Marshall Energy Company
MPE	Ministry of Public Enterprises
NDB	National Development Bank
OECD	Organisation for Economic Co-operation and Development
OPSG	Office of Public Sector Governance
PBMA	Public Bodies Management and Accountability Act
PCJ	Petroleum Corporation of Jamaica
PMB	People's Microbank
PNG	Papua New Guinea
PPP	public–private partnership
ROA	return on assets
ROE	return on equity

SAL	Solomon Airlines Limited
SCI	statement of corporate intent
SCO	statement of corporate objectives
SIBC	Solomon Islands Broadcasting Corporation
SIEA	Solomon Islands Electricity Authority
SIPA	Solomon Islands Port Authority
SIWA	Solomon Islands Water Authority
SML	Sasape Marina Limited
SOE	state-owned enterprise
TACV	Transportes Aéreos de Cabo Verde (Cabo Verde Airlines)
TCC	Tonga Communications Corporation
UTOS	Unit Trust of Samoa

CURRENCIES

$	Cabo Verdean escudo
F$	Fijian dollar
FY	fiscal year as defined by each country
J$	Jamaican dollar
K	Papua New Guinean kina
Rs	Mauritian rupee
SI$	Solomon Islands dollar
ST	Samoan tala
T$	Tongan pa'anga
$	United States dollar

EXECUTIVE SUMMARY

The state-owned enterprise (SOE) portfolios in the nine island economies participating in this study are dominated by infrastructure service providers (e.g., airports, seaports, power, water, sanitation, broadcasting, postal services, and telecommunications), but also include a range of other commercially oriented undertakings such as transport and banking. The study reveals that, while SOEs are often established to address perceived market failures or increase accountability in public service delivery, these goals are rarely achieved. None of the nine SOE portfolios produced a sufficient return to cover capital costs between 2002 and 2012. Only five produced average returns on assets and equity above zero over this period.

State-Owned Enterprise Portfolio Performance Indicators

Country	Average Return on Assets FY2002–FY2012 (%)	Average Return on Equity FY2002–FY2012 (%)	Contribution to GDP 2012[a] (%)
Cabo Verde (2008–2012)	(3.1)	(17.4)	3.6
Fiji	0.5	1.0	3.8
Jamaica	(3.7)	(55.6)	1.5
Marshall Islands	(5.6)	(12.6)	7.5
Mauritius	1.9	4.4	3.1
Papua New Guinea	3.3	5.8	2.4
Samoa	0.1	0.1	4.3
Solomon Islands	(1.3)	(6.1)	3.5
Tonga	3.2	5.2	6.0

( ) = negative, FY = financial year, GDP = gross domestic product.

[a] World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=worlddevelopment-indicators

Source: Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

In most countries, these low returns are achieved despite subsidized capital, monopoly market power, and ongoing government cash transfers. The low returns on SOE investment dampen economic growth. Despite governments' sizeable investments in the SOEs, they contribute only 1.5%–7.5% to gross domestic product (GDP)[1] in the benchmarked countries.

The study shows that low SOE returns are not unique to the Pacific (nor island economies), and are common throughout the developing and developed world. Chronic SOE portfolio underperformance highlights a fundamental flaw in the SOE model: it is not an effective long-term ownership structure. While the SOE model attempts to replicate private ownership demands and dynamics, it never truly replaces the market disciplines that private firms face. As long as SOEs remain under majority public ownership, politicians will avoid commercial decisions with potential short-term political costs.

Policy makers around the world are aware of SOEs' chronic underperformance, fiscal costs, and negative impact on growth and poverty alleviation. Consequently, efforts to reform SOEs have been ongoing for decades. This experience demonstrates that privatization, supported by robust regulatory arrangements, is the most effective

[1] SOE contribution to GDP is calculated by adding SOE earnings before depreciation and total wage expense, and dividing by GDP.

mechanism for long-term improvements in state assets' productivity. However, full privatization is not always politically feasible nor the most suitable reform mechanism; partial privatization (public listings, joint ventures, and public–private partnerships (PPPs)) can also help improve SOE performance.

While the nine countries have made important progress toward placing their SOEs on a more commercial footing, much more needs to be done. Key milestones between 2007–2014 include:

Cabo Verde: strengthening legal frameworks for SOEs in 2009–2010; establishing (ongoing) performance contracts with profitability and efficiency targets for the five largest SOEs; and developing an operating concession for the largest SOE port.

Fiji: corporatizing the Water Authority, Roads Authority, and Government Printery and Stationery Department; privatizing Fiji Dairy and preparing privatization options for Copra Millers and the Government Printery; implementing an operations and maintenance contract for Suva and Lautoka ports; and preparing three SOEs for listing on the Fiji Stock Exchange.

Jamaica: selling Air Jamaica in 2011 (this SOE contributed 75% of all portfolio losses while under government ownership); and, in 2012, updating the privatization policy, begin strengthening the Public Enterprise Division, and amending the Corporate Governance Framework for Public Bodies (first introduced in 2011).

The Marshall Islands: restructuring Marshall Energy Company with losses reduced by over two-thirds in 2010–2012; approving an SOE reform policy in 2012; and introducing the resulting SOE Bill into Parliament in 2013.

Mauritius: restructuring seven SOEs in 2012–2013, with a further four planned during 2014; creating the Office of Public Sector Governance in 2010; passing amendments in 2009–2012 to strengthen the Statutory Bodies (Accounts and Audit) Act 1972; and strengthening the PPP framework with plans to award two PPPs in 2014.

Papua New Guinea: approving a comprehensive community service obligations (CSO) policy in 2013 for implementation in 2014; endorsing draft PPP legislation in 2013; amending the Independent Public Business Corporation (IPBC) Act in 2012, resulting in improved SOE oversight; publishing IPBC accounts in 2011; and commencing the formulation of a new SOE policy framework.

Samoa: privatizing Samoa Broadcasting Corporation in 2008 and SamoaTel in 2010; establishing the Independent Selection Committee in 2010 to manage SOE director selection; appointing 180 new directors to SOE boards and removing elected officials following the Composition of Boards of Public Bodies Act 2012; and preparing Agriculture Stores Corporation for privatization.

Solomon Islands: divesting four SOEs since 2008; enacting the SOE Act in 2007 and supporting regulations in 2010; restructuring three major SOEs since 2010 and approving tariff increases for the water and power SOEs; completing CSO contracts for selected SOEs; and integrating the process into the 2013 and 2014 budgets.

Tonga: privatizing Leiola Duty Free in 2007; liquidating three SOEs; awarding six CSO contracts, two to the private sector; implementing skills-based SOE director selection in 2013; strengthening the SOE Act in 2010; and publishing SOE results in local newspapers from 2010.

Together with decades of international SOE reform experience, this study provides very clear lessons:

- As long as SOEs remain under government control, the risks of political interference and noncommercial decision making remain high.

- Governments have tried to address this fundamental flaw by creating legal, governance, and monitoring frameworks to mimic the conditions and incentives faced by private sector firms. Comprehensive SOE frameworks only lead to improved SOE performance if the political will to implement them exists.
- SOEs perform best in an environment supporting full commercial orientation, with strong governance, performance incentives, and hard budget constraints. Each of the nine countries has some elements of this, but all depend on political support for implementation.
- SOE performance deterioration is directly linked to weakened political commitment to protect and enforce the commercial imperative.

This study demonstrates the significant economic costs generated by poor SOE management, and the benefits resulting from reform. Ensuring SOEs are commercial and accountable frees scarce resources, enabling them to start contributing to economic growth, and leading to increased investment and an expanded private sector to drive this growth. The remarkable turnaround in Solomon Islands is a compelling illustration.

I. INTRODUCTION

This study reviews the historical financial performance of state-owned enterprises (SOEs) in selected island economies, identifies the drivers of performance, and outlines successful reform strategies to inform future policy action. The study examines SOE performance and reform efforts in nine countries: six from the Pacific region (Fiji, the Marshall Islands, Papua New Guinea, Samoa, Solomon Islands, and Tonga) and, for the first time, three from outside the Pacific (Cabo Verde, Jamaica, and Mauritius). Countries participating in prior studies in 2009, 2011, and 2012 requested that the study be regularly updated, and that other countries be invited to participate. This study responds to this request.

Participating countries were selected based on (i) their willingness to share their SOE financial accounts, (ii) the degree of reliability of these accounts, and (iii) the comparability of the SOE portfolios. While the countries vary significantly in size, population, and growth rates (Table 1), they are considered comparable due to their history of SOE reform and broadly similar SOE portfolios.

In this study, "SOE" refers to public enterprises, commercial statutory authorities, government commercial companies, and public trading bodies that are majority-owned by the state. All are corporatized and—with few exceptions—have a for-profit mandate. Only these entities are included in this benchmarking study. Mutual financial institutions, such as insurance companies and provident funds, are excluded as their shares are owned by their contributors, not the government. Some resource and petroleum SOEs, held and managed outside of the SOE monitoring units, have also been excluded. A detailed list of the included SOEs is provided in Appendix 2.

Financial data are provided from 2002 through 2012, the most recent fiscal year available. The study was prepared with the active support of the ministries of finance or public enterprises in each of the survey countries. Each ministry provided audited financial information on its SOEs, copies of SOE legislation, and completed a questionnaire broadly describing its SOE monitoring practices and governance arrangements. This information was then discussed with each agency for further clarification, before being assessed comparatively across the nine countries.

The study also explores broader international experience with SOE reform, identifies what has or has not worked, and highlights the key elements of successful policies. While the primary focus is on the comparative financial performance of the nine SOE portfolios, the study also looks at the underlying legislative frameworks, monitoring structures, governance arrangements, and the extent and nature of parliamentary oversight, as these factors can have an impact on the performance of the SOEs.

Table 1: Survey Country Economic Indicators

Country	Population (Total), 2012	GDP (current $), 2012	GDP per Capita (current $), 2012	GDP per Capita Growth (average annual %) 2002–2012
Cabo Verde	494,401	1,827,021,562	3,695	6.29
Fiji	874,742	3,907,563,305	4,467	1.39
Jamaica	2,712,100	14,755,051,129	5,440	(0.36)
Marshall Islands	52,555	182,400,000	3,471	1.38
Mauritius	1,291,456	10,486,037,634	8,120	3.85
Papua New Guinea	7,167,010	15,653,921,367	2,184	5.03
Samoa	188,889	683,719,606	3,620	2.35
Solomon Islands	549,598	1,008,424,232	1,835	5.24
Tonga	104,941	471,575,497	4,494	1.31

( ) = negative, GDP = gross domestic product.
Source: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators

The study's preliminary findings and recommendations were discussed with ministers and heads of departments of each of the participating countries at a Leaders Seminar in Sydney, Australia, in March 2014. This seminar provided a unique opportunity to share experiences and identify effective reform strategies. All participants at the seminar endorsed the study's findings and recommendations for broader publication.

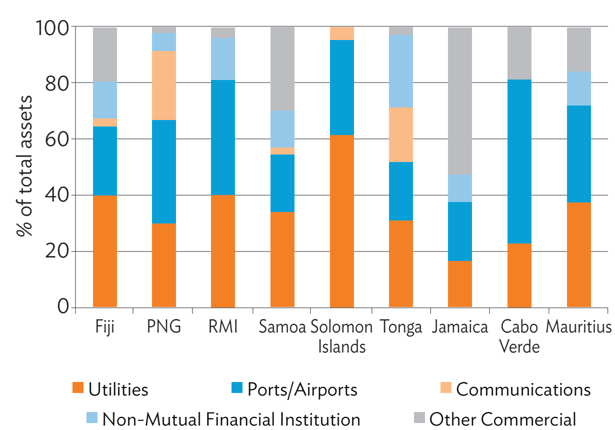
II. PROFILE AND ECONOMIC IMPACT OF THE STATE-OWNED ENTERPRISE PORTFOLIOS

A. PROFILE

The state-owned enterprises (SOEs) in this study are primarily engaged in two broad activities. These are the delivery of core public infrastructure services—airports, seaports, power, water, sanitation, broadcasting, postal services, and telecommunications—and a range of other commercially oriented undertakings such as transport, banking, food processing, property development, tourism, agriculture, oil, and gas. In eight of the nine countries, infrastructure SOEs dominate the portfolio, representing 52% to 96% of total assets in 2012 (Figure 1). Only Jamaica has a large percentage of noninfrastructure SOEs (62%).

Infrastructure SOEs are often forced to provide services on noncommercial terms. These subsidized activities, also known as community service obligations (CSOs), focus on delivering services to remote populations or providing services at reduced prices to selected customer groups. If properly contracted and funded, delivering these CSOs should not reduce the SOEs' profitability. The reality, however, is that CSOs are haphazardly imposed, poorly costed, and generally underfunded. These CSOs depress SOE profitability, contribute to inefficient resource allocation, and impair the government's ability to assess whether the CSOs provide value for money or achieve the outcomes sought.

Figure 1: Composition of State-Owned Enterprise Portfolios, FY2012



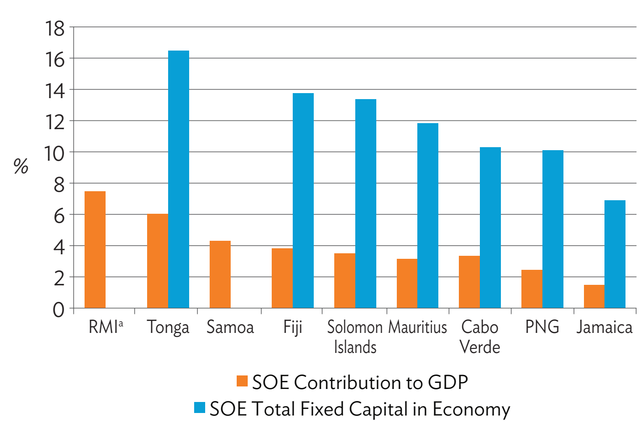
FY = financial year, PNG = Papua New Guinea, RMI = Republic of the Marshall Islands, SOE = state-owned enterprise.

Sources: Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

B. ECONOMIC IMPACT

Investments in SOEs are substantial, yet their contribution to gross domestic product (GDP) remains low. SOEs control 7%–17% of total fixed capital in each country yet contributed only 1.5%–7.5% to GDP in 2012 (Figure 2).[1] Government ownership has resulted in low productivity, which has damaged the growth rate of the economy as a whole, both directly and indirectly. First, SOEs themselves are often poorly managed, which has a direct impact on the productive use of the resources they tie up. Second, the outputs they produce are often of low quality and high cost but essential for commerce

Figure 2: Percentage of Total Fixed Capital Controlled by State-Owned Enterprises vs. Contribution to Gross Domestic Product, FY2012



FY = financial year, GDP = gross domestic product, PNG = Papua New Guinea, RMI = Republic of the Marshall Islands, SOE = state-owned enterprise, vs. = versus.

[a] SOE total fixed capital in economy data unavailable for RMI and Samoa.

Sources: ADB. 2013. *Key Indicators for Asia and the Pacific 2013.* Manila; ADB estimates; World Bank. World Development Indicators http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

[1] Due to data deficiencies, there is a large margin for error in these calculations. However, even in using the most optimistic estimates in a sensitivity analysis of the capital output ratio for countries in the sample, over a 10–year period, it appears that the low productivity of SOEs could have resulted in 10%–20% reduction in GDP. This is a very large economic cost imposed on this study's sample countries.

(e.g., utilities, transport infrastructure) which, in turn, adversely affects the private sector. Both reduce long-run growth.

SOEs also reduce growth by crowding out the private sector and dampening the competitiveness of domestic industries. When SOEs compete with private sector companies, they often do so on a favored basis—making it difficult for private sector competitors to invest and grow. Although private sector firms are generally more efficient and are not burdened with CSOs, SOEs enjoy a competitive advantage in three key areas:

- **Preferred access** to government contracts;
- **Subsidized capital,** with lower SOE debt and equity costs than private firms', allowing them to remain marginally profitable despite being less efficient than their private competitors; and
- **Monopoly** services provision, in some cases.

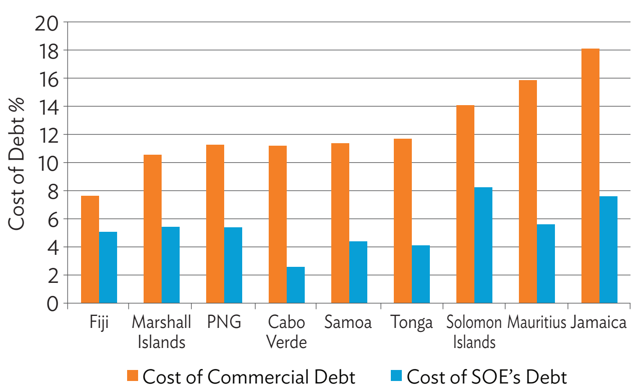
Subsidized debt, like subsidized equity, creates economic distortions. The interest rates SOEs pay on their debt are substantially below commercial rates (Figure 3). The low financing costs are a result of

- explicit and implicit government guarantees, and
- soft loans provided by government entities or on-lent from donors.

SOEs benefit from ongoing government equity contributions. These are typically provided to finance assets, retire debt, or simply absorb accumulated losses. During FY2003–FY2012, total government transfers to SOEs exceeded profits in five countries in this survey (Figure 4). This both distorts the economies, and contributes to fiscal deficits. In only four countries did governments receive more from their SOEs via dividends than the value of government transfers.[2] Cabo Verde, the Marshall Islands, and Samoa received transfers ranging from the equivalent of nearly 1% of GDP, to over 5% of GDP (Figure 5).

SOEs can be major contributors to macroeconomic instability. Loss-making SOEs create an ongoing strain on public finances. Jamaica and Cabo Verde, among the poorest-performing SOE portfolios in our benchmarking sample, had the highest levels of government debt to GDP in 2012 (146% and 86%, respectively). Four countries (Cabo Verde, the Marshall Islands, Samoa, and Solomon Islands) with the highest levels of government transfers to SOEs as a percentage of GDP, also have the highest levels of government expenditure to GDP (Figure 6).

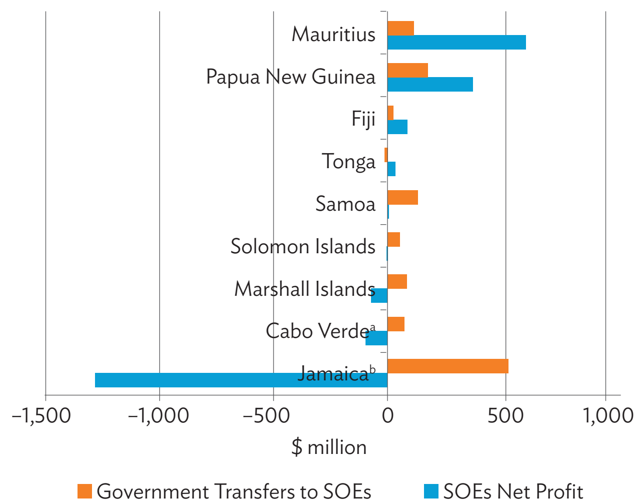
Figure 3: Average Cost of State-Owned Enterprise Debt vs. Commercial Debt Rate, 2002–2012



PNG = Papua New Guinea, SOE = state-owned enterprise, vs. = versus.

Sources: International Monetary Fund. International Financial Statistics; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; PNG: Bank of Papua New Guinea, and Independent Public Business Corporation; Solomon Islands: Ministry of Finance.

Figure 4: Total Government Transfers to State-Owned Enterprises vs. Total State-Owned Enterprise Net Profits, FY2003–FY2012



FY = financial year, SOE = state-owned enterprise, vs. = versus.

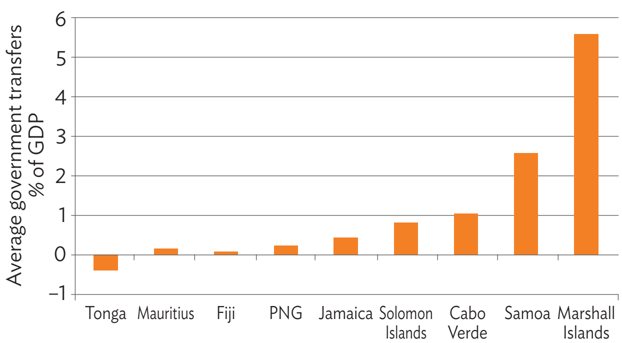
[a] Since 2008.

[b] Since 2003.

Sources: Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

[2] Fiji, Mauritius, PNG, and Tonga.

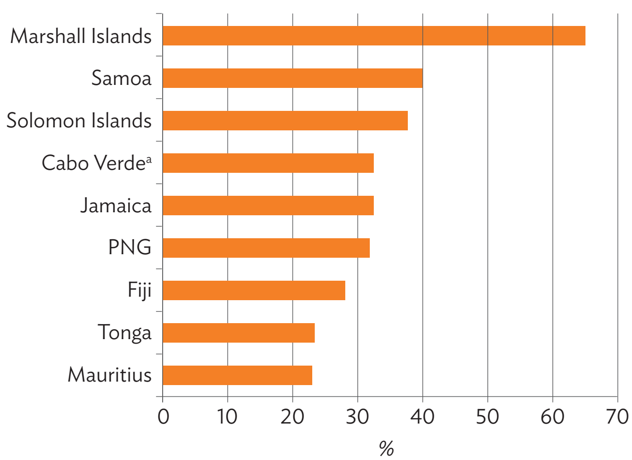
Figure 5: Average Government Transfers to State-Owned Enterprises as % of Average Gross Domestic Product, FY2003–FY2012



FY = financial year, GDP = gross domestic product, PNG = Papua New Guinea.

World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

Figure 6: Average General Government Expenditure as % of Gross Domestic Product, FY2002–FY2012



FY = financial year, PNG = Papua New Guinea.

[a] Since 2008.

Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; International Monetary Fund.

Table 2: Ease of Getting Electricity

Country	Rank[a]	Time to connect (days)	Cost (% of income per capita)
Papua New Guinea	24	66	57.5
Tonga	30	42	94.4
Samoa	37	34	783.6
Mauritius	48	84	281.1
Marshall Islands	77	67	729.5
Fiji	81	81	1,835.3
Solomon Islands	130	160	2,113.7
Jamaica	132	96	540.6
Cabo Verde	151	88	888.0

[a] Rank among 189 countries, where 1 is the most and 189 is the least conducive environment to starting and operating a business.

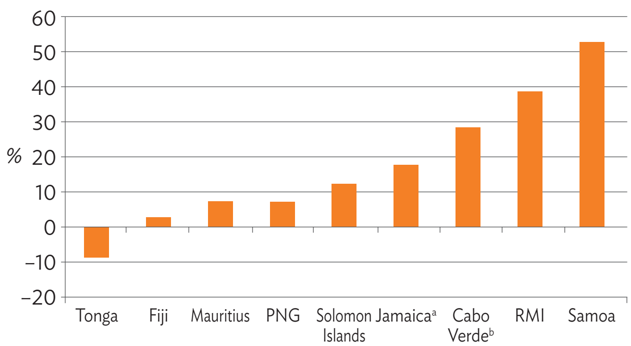
Source: International Finance Corporation and the World Bank Group. Doing Business 2014. http://www.doingbusiness.org/rankings

Monopolistic SOEs increase the costs of doing business. SOEs are the sole providers of a range of core infrastructure services in the benchmarked countries. The continued lack of competition or effective regulation results in higher prices and poor service delivery for users. In all surveyed countries, only SOEs provide power transmission and distribution services, water distribution, and airport and seaport management. In some countries, only SOEs provide power generation. This results in comparatively high costs and often cumbersome procedures for getting electricity, as illustrated in the 2014 Doing Business Report (Table 2).[3] Cabo Verde, Fiji, Jamaica, Mauritius, and now Papua New Guinea (PNG) are introducing greater private sector participation in providing these core infrastructure services. This process should be accelerated.

Ongoing investment in underperforming SOEs has both direct and indirect costs to the economy. By utilizing scarce resources in inefficient and loss-making public enterprises, they drain funds away from social sectors. During FY2003–FY2012, the value of government transfers to SOEs in Samoa equaled 53% of government expenditure on public health services, the highest opportunity cost of the benchmarked countries (Figure 7). It is an important indicator of the choices that governments make when propping up loss-making SOEs.

[3] This indicator tracks the procedures, time, and cost required for a business to obtain a permanent electricity connection for a newly constructed warehouse.

Figure 7: Cumulative Government Transfers to State-Owned Enterprises as % of Total Public Health Expenditure, FY2003–FY2012



FY = financial year, PNG = Papua New Guinea, RMI = Republic of the Marshall Islands.

[a] Since 2004.

[b] Since 2009.

Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises

C. STATE-OWNED ENTERPRISE FINANCIAL PERFORMANCE

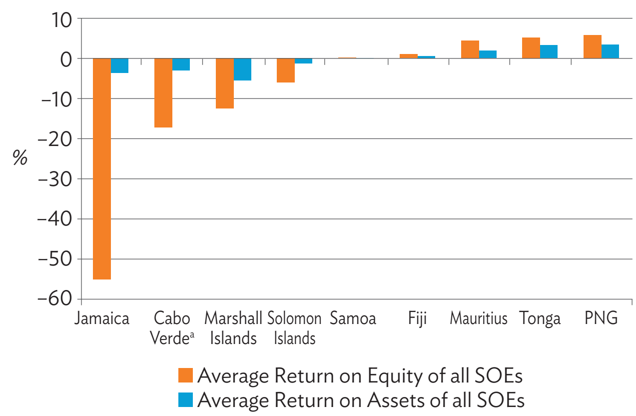
The financial performance of most SOE portfolios is weak. None of the SOE portfolios in the benchmarking survey produced a sufficient return to cover capital costs. Only five have produced average returns on equity (ROE) and assets (ROA) above zero over FY2002–FY2012 (Figure 8, Table 3). PNG, Tonga, Mauritius, and Fiji have ROAs averaging 3.3%, 3.2%, 1.9%, and 0.5%, respectively. The remaining countries had close to zero, or negative ROA.[4] PNG, Tonga, and Mauritius had the highest ROEs for the period, averaging 5.8%, 5.2% and 4.4%, respectively.[5]

ROA is improving in some countries in our sample. There is an upward trend in the average profitability of four of the nine SOE portfolios since 2010: Fiji, PNG, Solomon Islands, and Tonga. The turnaround in Solomon Islands has been dramatic, with the portfolio surging from an ROA of –12% in FY2008, to 10% in FY2012 (Figure 9). The Solomon Islands portfolio's return on equity in FY2012 was 15%, the best performance

[4] SOE financial data for Cabo Verde covers 2008–2012 only; for all other countries, the survey covers 2002–2012.

[5] Both ROA and ROE are important indicators of how efficiently SOEs use their capital resources, but differ depending on how much debt is used to finance operations.

Figure 8: Average Return on Equity and Assets of State-Owned Enterprise Portfolios, FY2002–FY2012



PNG = Papua New Guinea, SOE = state-owned enterprise.

[a] Since 2008.

Sources: Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

Table 3: State-Owned Enterprise Portfolio Profitability Indicators

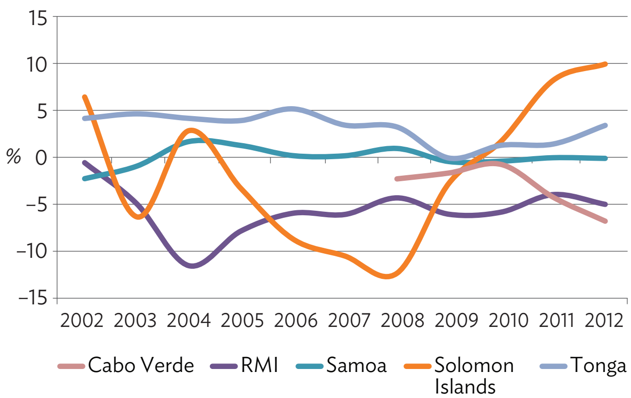
Country	Average Return on Equity FY2002–FY2012 (%)	Average Return on Assets FY2002–FY2012 (%)
Cabo Verde (2008–2012)	(17.4)	(3.1)
Fiji	1.0	0.5
Jamaica[a]	(55.6)	(3.7)
Marshall Islands	(12.6)	(5.6)
Mauritius	4.4	1.9
Papua New Guinea	5.8	3.3
Samoa	0.1	0.1
Solomon Islands	(6.1)	(1.3)
Tonga	5.2	3.2

( ) = negative, FY = financial year.

[a] Air Jamaica accounted for 75% of the portfolio losses over the 2002–2012 period; without Air Jamaica, the average ROE and ROA of the Jamaica portfolio would have been –11% and –2%, respectively.

Source: Cabo Verde: Ministry of Finance and Planning; Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

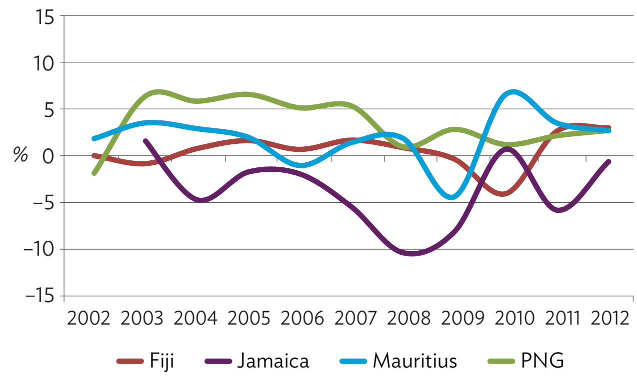
Figure 9: Average Return on Assets of State-Owned Enterprise Portfolios (Cabo Verde, the Marshall Islands, Samoa, Solomon Islands, and Tonga), GDP < $2 billion, FY2002–FY2012



FY = financial year, GDP = gross domestic product, RMI = Republic of the Marshall Islands.

Sources: Cabo Verde: Ministry of Finance and Planning; Marshall Islands: annual economic statistics tables, and annual SOE audit reports; Samoa: State-Owned Enterprise Monitoring Unit; Solomon Islands: Ministry of Finance; Tonga: Ministry of Public Enterprises.

Figure 10: Average Return on Assets of State-Owned Enterprise Portfolios (Fiji, Jamaica, Mauritius, and PNG), GDP > $2 billion, FY2002–FY2012



FY = financial year, GDP = gross domestic product, PNG = Papua New Guinea..

Sources: Fiji: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism; Jamaica: Public Enterprise Division, Ministry of Finance and Planning; Mauritius: Office of Public Sector Governance; PNG: Independent Public Business Corporation.

among the countries surveyed. This turnaround resulted from financial restructuring of the largest SOEs, improved collections, privatization of loss-making SOEs, and renewed efforts to implement the SOE Act requiring SOEs to operate on strict commercial principles.

Policy makers around the world are well aware of SOEs' chronic underperformance, fiscal costs, and negative impact on growth and poverty alleviation. As a result, efforts to reform SOEs are intensifying. This study identifies the drivers of improved SOE performance, drawing on global experience as well as the specific measures undertaken by the island economies benchmarked in this study.

III. COUNTRY DIAGNOSTICS

This section provides an overview of the state-owned enterprise (SOE) portfolios in each of the survey countries, a review of the history and recent attempts at reform, and key features of the legal, governance and monitoring frameworks. A financial snapshot of the SOEs that make up each country's portfolio is in Appendix 2.

A. CABO VERDE

SOEs are responsible for delivering services essential to Cabo Verde's competitiveness. The country's nine islands depend on SOEs for electricity, water, and transport—vital inputs for the tourism industry, as well as the transport of goods of services. The government has a controlling interest in 18 SOEs.[6] Six SOEs account for 93% of the portfolio's assets, 91% of the revenue, and 87% of the profits. These SOEs are providers of port, airport, air transport, water, electricity, and housing services. They employ more than 2,000 workers. The importance of the SOE services compels the state to provide financial assistance, creating a moral hazard. During FY2008–FY2012, the state transferred an estimated $75 million to the SOEs.

Table 4: Cabo Verde Key Indicators

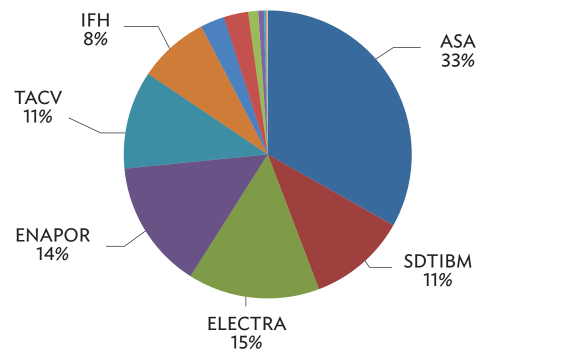
Population (total), 2012	494,401
GDP (current $), 2012	1,827,021,562
GDP per capita (current $), 2012	3,695
Population density (persons per km^2), 2012	123
Total surface area (km^2)	4,030
Number of islands	18
Number of SOEs included in this study	14

GDP = gross domestic product, km^2= square kilometer, SOE = state-owned enterprise.

Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Cabo Verde's SOE portfolio is chronically loss making. The portfolio averaged a –3.1% return on assets and –17.4% return on equity from FY2008–FY2012: 4 of the 14 SOEs had negative shareholder funds in 2012. One of the largest SOEs, the National Airports and Air Safety Company (ASA), has

Figure 11: Cabo Verde State-Owned Enterprise Portfolio Assets, FY2012 ($53 million)

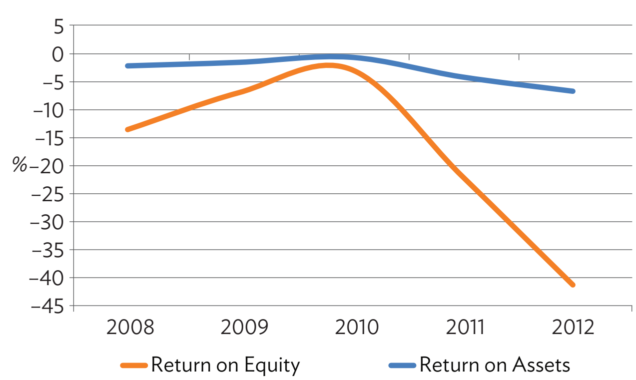


ASA = Empresa Nacional de Aeroportos e Segurança Aérea (National Airports and Air Safety Company), $ = escudo, ELECTRA = Empresa de Electricidade e Agua (Electricity and Water Company), ENAPOR = Empresa Nacional de Administração Dos Portos (National Ports Administration Company), FY = financial year, IFH = Imobiliária, Fundiária e Habitat (Real Estate, Land and Habitat), SDTIBM = Sociedade de Desenvolvimento Turístico das Ilhas Boa Vista e Maio (Tourism Development Corporation of the Boa Vista and Maio Islands), TACV = Transportes Aéreos de Cabo Verde (Cabo Verde Airlines).

Source: Ministry of Finance and Planning.

generated most of the portfolio's profits during this period, with Cabo Verde Airlines (TACV) and the Electricity and Water Company (ELECTRA) contributing most of the losses. The government has guaranteed the debt of both of these SOEs, further adding to its growing contingent liability balance estimated at 11.5% of gross domestic product (GDP) in 2010.[7]

Figure 12: Cabo Verde State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2008–FY2012



FY = financial year.

Source: Ministry of Finance and Planning.

[6] Only 14 of these 18 SOEs provided financial accounts for the purposes of this study; only these 14 have been included in the financial analysis.

[7] Based on a 2010 government report on the liabilities of six SOEs.

TACV and ELECTRA have been undergoing restructuring for many years. Strategies to improve the financial and operational performance have included privatization (ELECTRA in 1999), renationalization (ELECTRA in 2007), and the strengthening of the regulatory environment. While ELECTRA has made some progress toward cost recovery and reduction in technical losses, TACV has been unable to attract private investment or rationalize its service offering. It continues to generate over $2 billion of losses annually. It also maintains high arrears to another SOE, ASA. The Government plans to restructure and privatize TACV in 2014, including the sale of its subsidiary businesses.

Cabo Verde has a long history of SOE reform, with some positive results. The first programs focused on privatization, and resulted in the sale of more than 27 SOEs in 1992–2004, including Cabo Verde Telecom and ELECTRA, and the two major commercial banks. During this period, the SOE portfolio was reduced from 50 to 23 fully controlled holdings. Broad political consensus and continuity allowed the program to continue for more than a decade, despite a weak regulatory framework that allowed public monopolies to become private monopolies. The second phase of reforms, after 2001, focused on enhancing economic regulation, liberalizing sectors to spur competition, and improving the business and investment climate.

The legal framework for SOEs was strengthened in 2009–2010, but suffers from poor implementation. SOEs operate under the commercial code, their own founding legislation, and the 2009 SOE Law[8] that consolidates the main SOE governance provisions. It includes rules related to reporting, disclosure, state oversight, and boards of directors. It subjects SOEs to the same rules of competition as all other companies in Cabo Verde and appoints the Minister of Finance and Planning as the shareholder representative, with the sector minister acting as the responsible minister. To supplement the SOE Law, the government issued three supporting laws in 2010:

i) a decree establishing good governance principles for SOEs, covering conflicts of interest, tenure of director mandates, and disclosure of information to the public;[9]

ii) the Public Management Law, covering the principles of governance and operations;[10] and

iii) the Public Manager Organic Law, establishing profiles and responsibilities for SOE managers.[11]

This legal framework provides a sound basis for SOE governance and oversight, but lacks a fundamental requirement for SOEs to operate profitably and seek full cost recovery for CSOs.

SOE oversight remains weak. The state SOE monitoring unit with SOE oversight within the Ministry of Finance and Planning, the Direcção de Serviço das Participadas do Estado (Directorate of Service of the State Shareholdings, or DSPE), lacks both authority and capacity. With its current status within the General Directorate for Treasury, DSPE is unable to effectively assist the Ministry of Finance and Planning exert its ownership role. SOE boards do not recognize DSPE authority, and its staff lack the training, experience, and seniority to properly discharge their responsibilities. Moreover, DSPE lacks essential monitoring instruments, such as updated SOE accounts, strategic plans, budgets, and quarterly reports. SOEs are not systematically preparing these, despite the legal requirement to do so. Without these instruments to establish financial and operational performance targets, monitoring cannot be effective.

The SOE director selection and appointment process does not yet fully comply with the new Code. The 2009 Law and Code of Good Governance Principles for SOEs

Box 1: ELECTRA—Chronicle of a Failed Privatization

To address the increasing needs of electricity services in the country and improve the performance of Empresa de Electricidade e Água (ELECTRA), the state-owned utility, the government signed a 50-year concession contract with Energias de Portugal (EDP) and IPE-Águas de Portugal (ADP) in 1999.

The private partners acquired 51% of ELECTRA and committed to investing $26 billion over the first 15 years of the concession. Tariff increases were integrated into the agreement to offset the costs of ongoing investment and allow a commercial return.

Conflicts quickly arose when political pressure, consumer dissatisfaction, and poor public communication on the public–private partnership arrangement led the government to deny the tariff increases. Multiple contractual disputes ensued, and very little investment was made to upgrade the power and water infrastructure. The concession was abandoned and the government re-nationalized ELECTRA in 2007.

ELECTRA has continued to struggle under public ownership, generating high levels of liabilities and delivering poor quality electricity supply. Cabo Verde ranked in 2011 as 131st out of 142 countries by the World Economic Forum. The Government has now placed the company on a performance improvement program, with the goal of achieving full cost recovery through tariff increases and productivity gains.

$ = escudo.

8 Law 47/VII/2009.

9 Resolution 26/2010, 31 May 2010.

10 Decree Law No. 6/2010, 22 March 2010.

11 Footnote 10.

include comprehensive regulations related to boards and the appointment of experienced directors. Compliance and enforcement, however, remains low. While no elected officials serve on any SOE boards, directors continue to be appointed based on political rather than commercial considerations, and few are held accountable for results. In all 18 SOEs, the chief executives sit on the board as the managing director, and only one has a performance-based contract.

The government is now focusing on two SOE reform strategies: public–private partnerships (PPPs) to improve service delivery, and renewed implementation of the governance framework. The PPP program is being launched in the ports sector, with a series of operating concessions for the seven main ports, starting with the largest one in Praia. The concessions will be purely operational, with the state continuing to finance infrastructure improvements. Once the main ports are tendered, the government will consider the packaging of smaller ports as operating concessions. The government has announced that PPPs will also be pursued in other core sectors such as airports, energy, and social services. This ambitious program recognizes that the private sector can operate major infrastructure assets more efficiently than the public sector. The government intends to roll out the program progressively, ensuring that regulatory mechanisms are in place to create the needed efficiency incentives. For those SOEs remaining under government control, management contracts are being implemented to better monitor performance targets. A contract has been signed with ELECTRA, and others are being readied for Empresa Nacional de Produtos Farmaceuticos (the National Pharmaceutical Product Company, EMPROFAC), the National Ports Administration Company (ENAPOR), Real Estate, Land and Habitat (IFH), and TACV.

The PPP program will require additional capacity to be successful. Cabo Verde has no legal and regulatory framework for PPPs, and only limited capacity and knowledge of the PPP process. ENAPOR has established an informal working group with the Ministry of Finance and Planning to prepare the port PPP projects, and plans to train dedicated PPP staff in the coming year. Substantial additional capacity will be required to ensure that PPP projects are bankable, tendered in a transparent and fully competitive way, and implemented according to the terms of the agreement. As in many countries embarking on PPP programs, establishing a clear set of rules, guidelines, and institutional authority for the process reduces risks and costs for all parties involved.

Implementation of the governance framework will require broad political support and substantial strengthening of the monitoring arrangements. This will include raising DSPE's and recruiting senior staff to manage it; developing ownership and monitoring policies and guidelines for SOEs; helping SOEs develop and implement strategic plans, budgets, and quarterly reports; and ensuring that SOE accounts are prepared on time and published. Further amendments to the SOE Law will be required to clarify the SOE's commercial mandate, and provide a mechanism for the commercial delivery of community service obligations (CSOs).

B. FIJI

Fiji's SOEs have a substantial impact on the economy, providing most infrastructure services. The portfolio's profitability remains very low, with an average ROA of 0.5% and ROE of 1.0% for FY2002–FY2012. Portfolio profitability has increased markedly since 2010, with an ROE of 5.9% in 2011 and 6.5% in 2012, much closer to the 10% target set by the government. This was largely driven by tariff increases, reduced fuel costs, and efficiency gains at the Fiji Electricity Authority (FEA), and by improved profitability at Air Pacific Limited (AirPac), Fiji Pine, and Airports Fiji Limited (AFL). Government transfers to the SOEs for 2002–2012 were comparatively low at $27 million, and only 0.1% of average GDP, although this does not include the F$291 million of government guarantees on SOE borrowings.[12]

Four SOEs dominate the portfolio. FEA, Fiji Development Bank (FDB), AirPac, and AFL comprise 71% of total portfolio assets. They contributed 87% of total profits in 2012. Interestingly, three of the five best-performing SOEs in the portfolio are those with a substantial private shareholding: FINTEL (average ROE 2002–2012: 16%); Air Terminal Services (average ROE 2002–2012: 11%); and

Table 5: Fiji Key Indicators

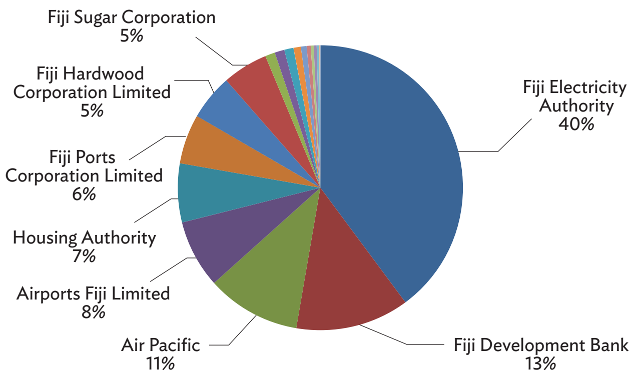
Population (total), 2012	874,742
GDP (current $), 2012	3,907,563,305
GDP per capita (current $), 2012	4,467
Population density (persons per km^2), 2012	48
Total surface area (km^2)	18,376
Number of islands	800
Number of SOEs included in this study	22

GDP = gross domestic product, km^2 = kilometer, SOE = state-owned enterprise.

Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

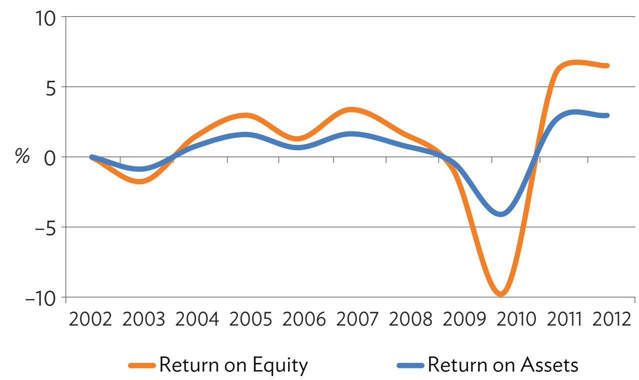
12 F$181 million ($100 million) provided to Air Pacific through the Fiji National Provident Fund (FNPF) and F$110 million guarantee for Fiji Sugar Corporation (FSC).

Figure 13: Fiji State-Owned Enterprise Portfolio Assets, FY2012 (F$2.6 billion)



F$ = Fijian dollar, FY = financial year.
Source: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism.

Figure 14: Fiji State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



FY = financial year.
Source: Ministry of Public Enterprises, Communications, Civil Aviation and Tourism.

AirPac (average ROE 2002–2012: 9%). The government owns just 51% of these three SOEs.

Fiji has been reforming its SOEs for over 20 years. The Public Enterprise Act in 1996 formalized the reform process. The government adopted a policy framework for SOE governance, management, and privatization in 2001, followed by a corporate governance framework in 2003. Fiji has been a regional leader in contracting out CSOs to the private sector, and continues to seek opportunities to privatize other government functions.

Progress in commercializing SOEs has been intermittent since 2006, but some restructuring has been undertaken. Key achievements include:

- corporatizing the Water Authority, Roads Authority, and Government Printery and Stationery Department;
- privatizing Fiji Dairy;
- merging Fiji Ships and Heavy Industry with Fiji Ports Corporation;
- appointing a Sugar Task Force to develop restructuring options for the Fiji Sugar Corporation (FSC), which ended the 2011 financial year with negative shareholders' funds of F$100 million;[13]
- identifying privatization options for Copra Millers and Government Printery and Stationery Department;
- preparing FEA for public listing, and contracting with a private operator to manage Suva and Lautoka ports;[14] and
- preparing AFL for a PPP.

Fiji's sound legislative, governance, and monitoring framework needs further strengthening. This could include:

- requiring all SOEs to achieve their cost of capital;
- strengthening director duties;
- refining CSO requirements and processes; and
- clarifying reporting and accountability provisions.[15]

Commercial Statutory Authorities (CSAs) should be subject to the same requirements as Government Commercial Companies (GCCs). The SOE Act differentiates between commercial SOEs (GCCs) and noncommercial SOEs (CSAs). The key difference between the two is that CSAs are not required to generate a profit and are not subject to the rules relating to CSOs. In practice the distinction between GCCs and CSAs is confusing. FEA, which accounts for 40% of the total portfolio assets, is a CSA and is therefore not required to operate profitably. In reality, FEA does operate commercially and makes significant profits but, as it is not subject to the CSO rules, the board withholds all profits and uses these surpluses to fund activities the board determines are CSOs. Withholding dividends and determining what are, and are not, CSOs are not decisions that a board should make—they are shareholder (ownership) or political decisions.

13 A F$110 million government guarantee and F$56.5 million government loan—advanced in 2011—allow FSC to continue operating.

14 The operator reported a 35% improvement in port efficiency in the first 2 months.

15 This could include lengthening the period covered by planning documents, removing ministers' authority to direct content, and publishing results against targets.

To strengthen SOE monitoring, the ownership monitoring team within the Ministry of Finance has been merged with the Ministry of Public Enterprises. Before January 2014, SOE ownership monitoring was divided between the Asset Management Unit (AMU) in the Ministry of Finance and the Ministry of Public Enterprises (MPE). The AMU was primarily responsible for the partially privatized SOEs, but there was significant duplication of activity with the MPE. Now that the merger is complete, ownership monitoring practices should improve.

Improved ownership monitoring should eliminate the need for monitoring staff to sit as board observers. To deal with weaknesses in ownership monitoring and the lack of quality and timely information from the SOEs, ownership monitoring staff sit as observers on SOE boards. This exposes the monitoring staff to conflicts of interest as they could be deemed directors, and it undermines the board's independence and accountability.

Sustainable improvement in SOE performance could be achieved with the implementation of the broader SOE reform program. Key actions would include:

- cementing the merger of the AMU and MPE ownership monitoring teams and rebuilding monitoring capacity;
- updating the SOE legislation to align it with international good practice;
- amending the PPP legislation and establishing a functioning PPP unit in the Ministry of Finance;
- developing a privatization pipeline;
- identifying opportunities to contract out current SOE activities and develop PPP opportunities;
- rebuilding board skills and competencies, implementing skills-based board selection and a board evaluation program;
- removing monitoring staff as board observers, strengthening board reporting practices, and holding directors accountable for results; and
- strengthening SOE reporting and transparency.

C. JAMAICA

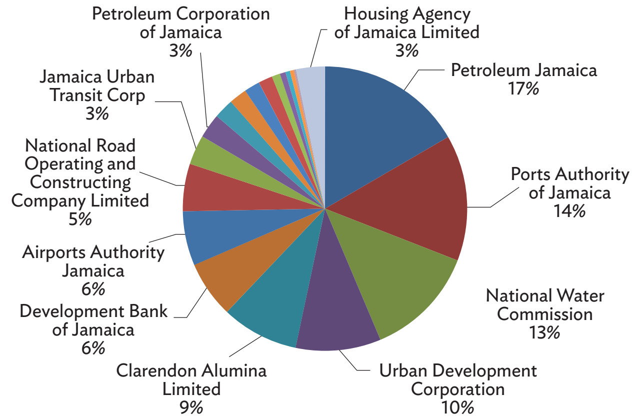
SOEs operate in almost every sector of the economy. They provide public transport, banking, airport, water, housing, ports, hotel, mining, and petroleum-related services. Only 12 of the 24 SOEs generated a net cumulative profit over FY2003–FY2012, with the largest losses attributable to Air Jamaica, Clarendon Alumina, National Road Operating and Constructing Company, National Water Commission, and the Sugar Company of Jamaica. The largest SOE, PetroJAM,[16] represents 17% of the total portfolio assets and, with the Port Authority of Jamaica, contributed the bulk of the portfolio's positive earnings. Jamaica has the highest proportion of non-infrastructure SOEs in the benchmarking sample, representing 53% of the total portfolio assets, and contributing 44% of the cumulative loss over FY2003–FY2012. These tend to be the SOEs that compete directly with the private sector, and their ability to continue operating at a loss crowds out private competitors.

Table 6: Jamaica Key Indicators

Population (total), 2012	2,712,100
GDP (current $), 2012	14,755,051,129
GDP per capita (current $), 2012	5,440
Population density (persons per km^2), 2012	250
Total surface area (km^2)	11,000
Number of islands	1
Number of SOEs included in this study	24

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

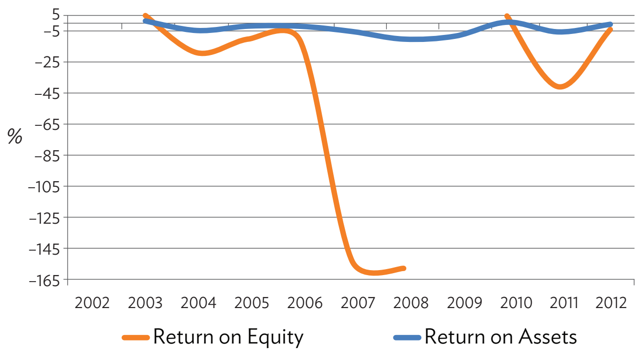
Figure 15: Jamaica State-Owned Enterprise Portfolio Assets, FY2012 (J$351 million)



FY = financial year, F$ = Jamaican dollar.
Source: Public Enterprise Division, Ministry of Finance and Planning.

[16] PetroJAM is a subsidiary of Petroleum Corporation of Jamaica (PCJ), but is not consolidated as part of PCJ's accounts. Other PCJ subsidiaries not consolidated and therefore separately included in the portfolio are Petrojam Ethanol Limited (PEL), Petroleum Company of Jamaica Limited (PETCOM), and Wigton Windfarm Limited (WWL).

Figure 16: Jamaica State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2003–FY2012[a]



FY = financial year.
[a] Jamaica's ROE could not be calculated in 2009 due to a negative equity balance.
Source: Public Enterprise Division, Ministry of Finance and Planning.

Jamaica's SOE portfolio is the poorest performer in the benchmarking sample. The average ROA and ROE[17] of the 24 SOEs in FY2003–FY2012 was –3.7% and –55.6%, respectively.[18] The portfolio generated positive returns on assets and equity in just 2 years over the past decade, 2003 and 2010. To absorb these losses and keep the SOEs operating, the government has injected almost $250 million[19] over this period, money which could have otherwise been spent on vital social services such as health and education. The SOE sector's low productivity has slowed economic growth, as illustrated by its low (1.5%) contribution to GDP in 2012.

During the mid-1990 financial crisis, the government's rescue of failed financial institutions, and the renationalization of previously privatized SOEs, resulted in an expanded SOE portfolio. Some failed financial institutions were managed by, or placed in, the Financial Sector Adjustment Company (FINSAC)—a state-owned bank. Many of these SOEs were subsequently divested, adding to the total of 100 divestments[20] between 1980 and 2012. There were 22 full or partial privatizations between 1999 and 2013. While the number of privatizations appears impressive, the potential fiscal benefits were undermined by the ongoing poor performance of those SOEs that remained under government ownership.

[17] If Air Jamaica were excluded, the portfolio average ROE 2003–2012 would be –9%.

[18] The 24 SOEs used in this benchmarking survey are a subset of the 195 entities known as "public bodies" in Jamaica. The 24 SOEs are the majority state-owned, for-profit and predominately self-financing entities.

[19] This figure does not include all the amounts transferred to SOEs through the government forgiving debt owed or assuming SOE's debt obligations to third parties. These are estimated to be substantial, but could not be obtained for this study.

[20] These divestments include the sale of government agencies, non-corporatized assets, and SOEs.

In 2012, the government updated its 1991 privatization policy to align it more closely with its public sector reform objectives. The Development Bank of Jamaica (DBJ), responsible for implementing the privatization program since 2006,[21] has a pipeline of 13 transactions comprising real estate assets, hotels, and SOEs. The policy supports continued privatization to allow the government to focus on its core mandate, and guides transaction processing and post-sale monitoring for partially privatized SOEs (Box 2).

The government has also signaled its commitment to PPPs, with Parliament approving a Policy and Institutional Framework for Implementation of a Public–Private Partnership Programme in 2012, and subsequent establishment of a PPP Secretariat in the DBJ.

The government's practice of underwriting failing and even privatized SOEs has created an important moral hazard. The experience of Air Jamaica (Box 3) and FINSAC illustrate this point. If SOEs are to operate commercially, they must be allowed to fail.

Box 2: Main Precepts of Government of Jamaica Privatization Policy

- Secure greater efficiency and competitiveness in the enterprises' operations;
- Reduce the drain on the Government of Jamaica's (GoJ) fiscal resources;
- Strengthen the GoJ's fiscal and debt management program;
- Accelerate the transfer of capital, technology, and management procedures;
- Widen the ownership base; and
- Maximize efficiency in providing public services through outsourcing, to deliver greater value for money.

Assets to target include

- those that form no part of the GoJ's core service obligations,
- assets not being used to provide social goods and services,
- those that can be more efficiently developed and operated with private capital and under private management,
- assets that unnecessarily burden taxpayers, and
- assets needed for providing public services that private firms can operate more efficiently—supplying services under contract to the GoJ.

[21] The National Investment Bank of Jamaica Limited was the implementing agency for the privatization program from 1991 to 2006.

Box 3: The Cost of Owning Air Jamaica

Air Jamaica (AirJAM) was established in 1963 as a joint venture with British and Trinidadian state airways. After years of losses, the Government of Jamaica (GoJ) acquired the company in 1980, yet the airline continued to generate losses for most of the next 14 years. In 1994, GoJ sold 70% of the airline to Jamaican and Canadian investors for $26.5 million, reserving 5% for employees. The GoJ retained 25% and responsibility for all accumulated liabilities. The following year, AirJAM made a small operational profit but the situation again deteriorated, with total losses of $100 million in 1997 and in 1998, forcing fresh capital injections of $50 million and $80 million in those 2 years. The poor performance was attributed to operating restrictions imposed by the United States (US) Federal Aviation Administration, and the airline's inability to increase efficiency and forge alliances with other carriers.

By 2004, liabilities to the government totaled close to $400 million and the airline was renationalized, with a plan to reduce the $60 million–$70 million annual losses through restructuring and downsizing. Instead, the loss increased to over $100 million annually, culminating in FY2010 (ends March 2010) at the equivalent of 1.8% of gross domestic product (GDP). In 2011—after a lengthy sales process—the government sold 84% of AirJAM to Caribbean Airlines Limited (CAL), the state-owned airline of Trinidad and Tobago. GoJ again retained responsibility for the accumulated debt of $940 million, as well as employee separation payments, air traffic liabilities, and contract termination payments. This totaled an additional $148 million.

Despite subsidized fuel from the government of Trinidad and Tobago, CAL continues to lose money on its AirJAM routes. CAL cannot compete with the 20 airlines servicing Jamaica, including Air Canada, US Airways, British Airways, American Airlines, and low-cost carriers. AirJAM's history illustrates the high risk of maintaining a state-owned airline. During its 50-year life, the airline has cost Jamaican taxpayers an estimated $1.5 billion (equivalent to 12% of GDP in 2009–2010).

The SOEs operate within a weak legislative framework. The primary SOE law, the Public Bodies Management and Accountability Act 2001 (PBMA Act),[22] is deficient in important areas, most notably: (i) there is no primary objective that requires the SOEs to operate commercially;[23] (ii) there are no provisions dealing with CSOs, and (iii) there is no statement establishing how the directors are to be held to account. The only commercial imperative in the Act is that the board must take "such steps as are necessary for the efficient and effective management of the public body." The SOE law and oversight practice do not differentiate between "commercial" and "noncommercial" SOEs—all are subject to the same performance targets and reporting requirements. The PBMA Act does include useful monitoring requirements, although actual practice falls short of the statutory requirements with delays in the production of SOE interim reports and audited financial statements.[24]

The governance arrangements do not support the commercial management of the SOEs. The Minister responsible for an SOE is the minister responsible for the sector within which the SOE operates and, as such, has a significant conflict of interest—being both the purchaser of the SOEs' outputs and the sector regulator. The sector minister is motivated to encourage the SOE to provide maximum goods and/or services at the lowest price or cost to beneficiaries. However, a commercially focused owner would focus on achieving an acceptable financial return—to compensate for risk—and to ensure the SOE's long-term organizational health. The responsible ministers' focus on the former largely explains the poor performance of Jamaica's SOEs.

The Public Enterprise Division (PED) within the Ministry of Finance and Planning manages the oversight of Jamaica's SOEs, yet its focus is primarily on fiscal oversight—not ownership.[25] The line or sector ministries undertake some ownership monitoring, supporting their "responsible minister". For the same reasons that sector ministers have a conflict of interest in overseeing SOEs, so too do the sector ministries. Consequently, there is no agency that can effectively act as SOE ownership monitor. A central SOE ownership monitor—reporting to a minister of SOEs—would strengthen the government's ownership oversight function.

The Corporate Governance Framework for Public Bodies, introduced in 2011 and amended in 2012, provides a strong basis for strengthening governance practices. The framework was developed to address the weaknesses in SOE governance, but insufficient personnel and funding—and absence of a dedicated ownership monitor—has resulted in patchy implementation. The Ministry of Finance and Planning has identified improved governance practices as a key driver

22 The act was amended in 2010.

23 The 2012 PBMA Regulations set dividend targets, but fall short of requiring SOEs to operate profitably.

24 Based on responses to the ADB questionnaire sent to all relevant sector ministries and the Ministry of Finance and Planning. In 2013, less than 50% of SOEs produced annual reports within the time frame set in the PBMA Act.

25 The PED was established in 1982 and restructuring commenced in 2012. Currently, it monitors 65 out of the 195 public bodies in Jamaica, but expects to monitor all 195 by September 2015. Its mission is to "develop policies and monitor adherence to policy guidelines that will lead to improved financial management practices in public bodies."

for improved SOE performance, and plans to introduce a code of conduct for directors as regulations to the PBMA Act. The adoption of a skills-based director selection process, improved board composition—directors with a proper mix of skills—and greater clarity in the role and responsibility of ministers, boards, and management are important reforms.

To achieve a sustainable improvement in SOE performance, Jamaica must strengthen its legal, governance, and monitoring framework. The framework must require

- SOEs to operate under a well-defined and transparent commercial mandate with accountability for results;
- directors and managers to face the same disciplines, challenges, and rewards as their private sector counterparts;
- SOEs to be fully and fairly compensated for CSOs;
- governments to contract the provision of CSOs directly with the private sector, where appropriate;
- a central SOE ownership-monitoring agency or ministry, reporting to a minister responsible for all SOEs; and
- the full implementation of the Corporate Governance Framework for Public Bodies.

D. THE MARSHALL ISLANDS

The Marshall Islands' SOE portfolio generated losses each year from 2002 to 2012, with an average ROA of –5.6% and ROE of –12.6%. The trend is a slight improvement over the –13.3% ROE for 2002–2010, yet still significantly drained the national budget. Four large SOEs dominated the portfolio: Marshall Island Ports Authority, National Telecommunications Authority, Marshall Islands Development Bank (MIDB), and Marshall Energy Company (MEC).

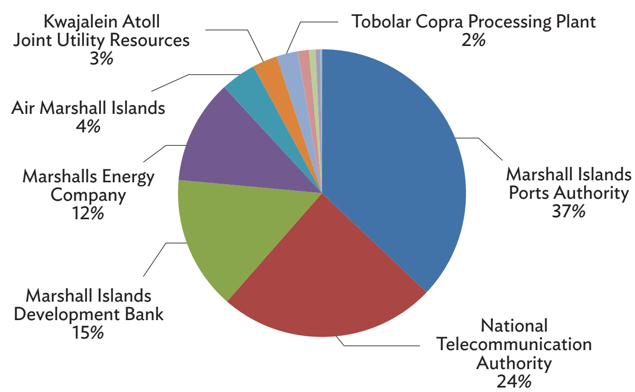
Table 7: The Marshall Islands Key Indicators

Population (total), 2012	52,555
GDP (current $), 2012	182,400,000
GDP per capita (current $), 2012	3,471
Population density (persons per km^2), 2012	292
Total surface area (km^2)	181
Number of islands	5; 29 atolls
Number of SOEs included in this study	11

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.

Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Figure 17: The Marshall Islands State-Owned Enterprise Portfolio Assets, FY2012 ($148 million)



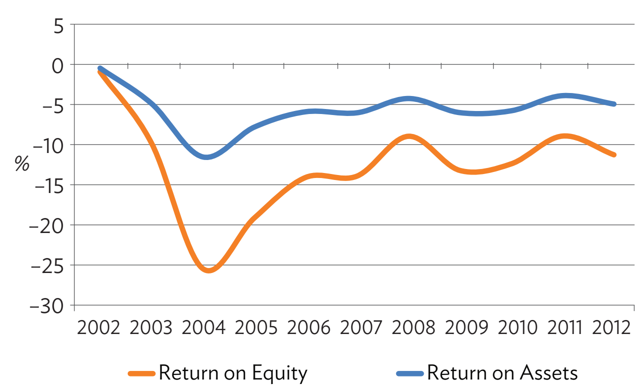
FY = financial year.

Sources: Annual State-Owned Enterprise Audit Reports; annual economic statistics tables (Republic of the Marshall Islands).

These four represent 88% of total SOE assets, with the Ports Authority alone accounting for 37%. MIDB is the only profitable SOE, achieving an average ROE of 4% for 2002–2012. Its comparatively better financial performance appears to be due to the board and management adopting a strong, independent commercial focus.

The restructuring plan for the MEC is starting to yield some benefits. MEC's operating losses were pulled back from $1.66 million in 2010 to $0.45 million in 2012.[26] The company still carries negative shareholder funds of $11.6 million, but is recovering. The board has adopted a Comprehensive Recovery

Figure 18: The Marshall Islands State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



Sources: Annual State-Owned Enterprise Audit Reports; annual economic statistics tables (Republic of the Marshall Islands).

[26] MEC reported a $2.1 million operating profit for FY2013.

Plan to (i) strengthen MEC and energy sector governance; (ii) improve organizational policies, performance, and capacity; and (iii) strengthen and stabilize company finances.

SOEs are sustained by a high level of government transfers—$85 million—and access to significantly discounted debt. Average government transfers to SOEs during FY2002–FY2012 were equivalent to 5.6% of average GDP, the highest in the benchmarking sample. The gap between commercial loan rates and the rates SOEs paid has increased from 5.8% in 2002 to 8.5% in 2012. The negative ROE and high level of ongoing government contributions drain money from much-needed social services, such as health and education. The net transfers paid to SOEs equate to 38.8% of the total public expenditure on health over the FY2002–FY2012 period.

The legislative, governance, and monitoring framework is very weak. There is no overarching SOE law. Most SOEs are established through their own Acts, which generally lack a commercial focus, robust director duties and obligations, and effective reporting and accountability mechanisms. There is no ownership monitor. The Ministry of Finance has fiscal oversight of the SOEs, and any ownership monitoring that is undertaken is left to the line or sector ministries.

The government adopted an SOE reform policy in 2012 that guided the SOE Bill drafted in 2013. The Bill, when enacted, will establish a robust legislative, governance, and monitoring framework. Implementation should substantially improve SOE financial and operational performance, particularly if it is accompanied by continued SOE restructuring.

E. MAURITIUS

SOEs are responsible for delivering services essential for Mauritius' competitiveness, and employ an estimated 36,000 workers. SOEs are active in almost every segment of the economy, providing power, water, transport, banking, agriculture, land development, and housing services. In 2012, the five largest SOEs accounted for 70% of the assets and 99% of the profit of the portfolio.[27]

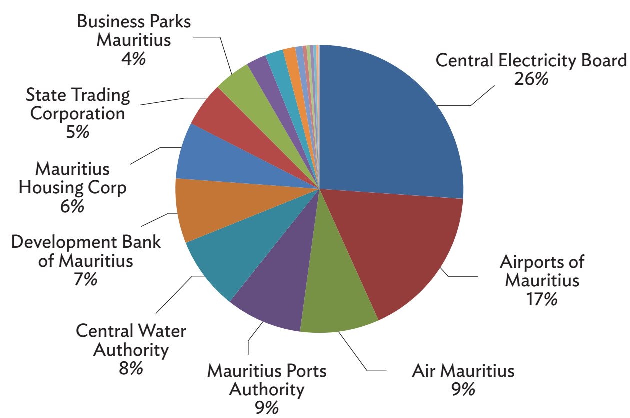
Of the 20 SOEs included in this benchmarking study, 8 are companies under the Companies Act while the remaining 12 are established by their own legislation. To be included in the SOE portfolio, the government must own and control at least 51% of the issued shares or, in the case of statutory bodies, have legal control. Many of the SOEs have mixed ownership, often with shares held by the government and other state-owned entities. Mauritius Telecom Limited has not been included in the portfolio, as the government controls just 33.45% of the shareholding. The remaining shares are owned by Group France Telecom–Orange (40%), State Bank of Mauritius through its wholly owned subsidiary SBM NFC Investments Limited (19%), and National Pensions Fund (6.5%).[28] Air Mauritius Limited (AML) is included in the portfolio; Air Mauritius Holdings Limited owns 51% of the shares in AML, which is then owned by the government (43.8%) and State Investment Corporation Limited (18.3%). The government owns 85% of the shares issued by the State Investment Corporation Limited.

Table 8: Mauritius Key Indicators

Population (total), 2012	1,291,456
GDP (current $), 2012	10,486,037,634
GDP per capita (current $), 2012	8,120
Population density (persons per km^2), 2012	636
Total surface area (km^2)	2,040
Number of islands	4
Number of SOEs included in this study	20

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Figure 19: Mauritius State-Owned Enterprise Portfolio Assets, FY2012 (Rs102 million)

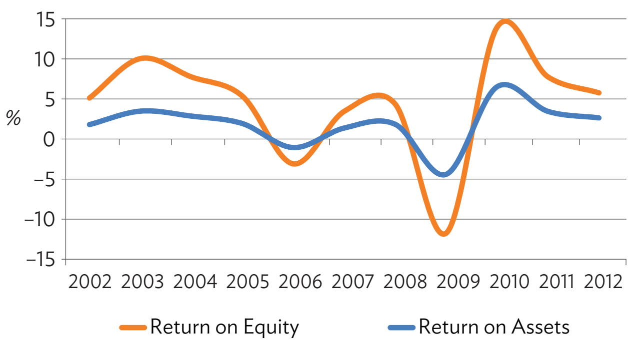


FY = financial year, Rs = Mauritian rupee.
Source: Office of Public Sector Governance.

27 In 2010, the International Monetary Fund (IMF) estimated that investment expenditure for the 15 largest SOEs was 8.5% of GDP, and total government transfers to the SOE portfolio were estimated at 2.7% of GDP.

28 The State Bank of Mauritius is listed on the Mauritius stock exchange. The major shareholders are general holding (42%), National Pensions Fund (19.1%), and State Insurance Company (17.1%).

Figure 20: Mauritius State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



FY = financial year.
Source: Office of Public Sector Governance.

The SOE portfolio generated an average ROA of 1.9% and ROE of 3.9% from FY2002–FY2012. Most SOEs suffer from low productivity and profitability. The 8 SOEs under the Companies Act generated 54% of the portfolio's total profit from FY2002–FY2012, and had an average ROE of 6.1% compared to the 12 SOEs established under their own legislation, which returned an average of –2.6% on equity. Airports of Mauritius generated 28.7% of the total profits of the portfolio in FY2002–FY2012, followed by Mauritius Ports Authority at 27.5%.

The Government's policy of providing guarantees on SOE debt has driven total contingent liabilities of the government to $864 million in 2012, or 8.2% of GDP. This policy is now being curtailed, which will drive up the costs of SOE borrowing from the average of 6% in FY2002–FY2012 (compared to 16% for private firms). To further reduce the government's exposure to unprofitable SOEs, it is merging some and restructuring others. Eleven SOEs have been identified as requiring immediate restructuring, and a further six have been merged into one. Seven SOEs were restructured in 2012 and 2013, and another four will be completed in 2014.

The SOEs operate under a comprehensive legislative framework. The Financial Reporting Act 2004 establishes the National Committee on Corporate Governance, with the role to establish binding governance requirements for public and private companies and, in particular, SOEs. The Act also establishes an Institute of Directors to "promote the highest standards of corporate governance, and of business and ethical conduct of directors serving on boards of companies and SOEs."[29] The Statutory Bodies (Accounts and Audit) Act 1972 stipulates that all non-company SOEs must produce 3-year strategic plans. The plan must be included in their annual report, and tabled in Parliament by the responsible minister.

Box 4: State-Owned Enterprises Restructured in 2012–2013

- Business Parks of Mauritius Limited
- Cyber Properties Investment Limited
- National Transport Corporation
- Agricultural Marketing Board
- National Housing Development Company
- Small and Medium Enterprises Development Authority
- Mauritius Meat Authority

Mauritius has taken important steps to strengthen the oversight of the SOE sector. In 2010, it created the Office of Public Sector Governance (OPSG) as a specialized monitoring and oversight unit under the Prime Minister's Office. However, ownership monitoring remains fragmented—sector ministers are responsible for SOEs operating in their economic sector, and the Committee on Corporate Governance is responsible for monitoring SOE governance. Implementation of improved governance and monitoring measures has started but remains difficult, as the OPSG has limited capacity.[30]

In addition to the governance reforms, the authorities are considering placing all SOEs under the Companies Act. This has already been done for a number of SOEs requiring restructuring, as the Companies Act allows a much greater range of restructuring measures than the SOEs' establishing legislation. PPPs are also being considered now that the PPP framework has been strengthened.[31] Two PPPs, one for road infrastructure and the other for renewable energy, are expected to be awarded in 2014. The transition to the Companies Act should facilitate the implementation of the Code of Corporate Governance, as there are no aspects of the Code which conflict with the Companies Act.[32]

29 Section 70 Financial Reporting Act 2004.

30 SOEs comply with 50%–60% of the code requirements.

31 Measures include the establishment of a PPP Unit, protocols for PPP project development between the Unit and sponsoring line agencies, and technical training.

32 Conflicts between the Code and the establishing legislation of some SOEs have inhibited implementation.

Sustainable SOE reforms will require placing all profit-oriented SOEs on a firm commercial footing, supported by a clear framework for CSOs and accountability mechanisms that create real incentives for performance. This framework would allow the government to continue to use SOEs to deliver public services, but would ensure that these services are delivered in a more efficient, sustainable manner. Full cost recovery would be required. This reform could be supported by the conversion of all SOEs to companies under the Companies Act or, alternatively, strengthening the existing SOE legislative framework. The strengthened legal framework should require that all SOEs

- have a primary objective to operate profitably;
- receive full compensation for all CSOs;
- hold the Board and management of SOEs accountable for results;
- prepare business plans and statements of corporate intent (SCIs),[33] and report regularly to OPSG; and
- operate on a level playing field with private firms.

A strengthened OPSG is needed to support SOE reform. The OPSG has a mandate to oversee the performance of the SOEs, yet needs additional resources, authority, and skills to do this effectively. Centralizing SOE ownership monitoring within OPSG, recruiting more specialized staff, and training existing staff would improve OPSG's effectiveness—as would wide public dissemination of SOE results. Combined with high-level support for its mandate, this will allow OPSG to play a critical role in improving the performance of the portfolio as a whole.

F. PAPUA NEW GUINEA

Papua New Guinea's (PNG) SOE portfolio saw a moderate improvement in performance in 2011 and 2012, but returns on assets and equity remain low. PNG's portfolio recorded the highest average ROA and ROE in the region between 2002 and 2012, but this masks a decline in performance since 2007. The portfolio ROE averaged 10.5% between 2003 and 2007, but fell to 3.4% in 2007–2012. In 2012, the SOE portfolios in Fiji, Solomon Islands, and Tonga outperformed the PNG portfolio—Solomon Islands' ROE (14.6%) was almost three times higher than PNG's (4.7%).

The assets controlled by PNG's SOEs have grown rapidly but evidence suggests that asset use is inefficient. Between 2002 and 2012, SOE assets grew at an average of 21.8% annually, more than double the rate of any other country in the study. SOEs contributed only 2.4% to GDP, suggesting inefficient capital utilization.

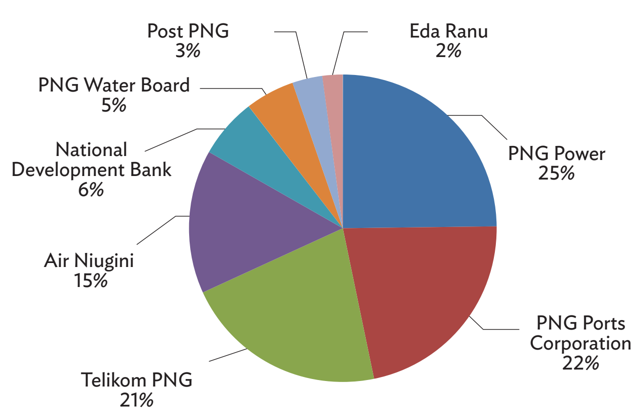
Table 9: Papua New Guinea Key Indicators

Population (total), 2012	7,167,010
GDP (current $), 2012	15,653,921,367
GDP per capita (current $), 2012	2,184
Population density (persons per km^2), 2012	16
Total surface area (km^2)	463,000
Number of islands	600; 1 mainland
Number of SOEs included in this study	8

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Asset growth is concentrated among the four largest SOEs—driven by government policy, favorable regulation, and strong economic growth. Air Niugini, PNG Ports, PNG Power, and Telikom are the four largest companies in the portfolio and account for 83% of SOE assets. Strong economic performance has stimulated demand for these SOEs' services and pushed up their land and buildings' values. The revaluation of existing assets accounted for 30% of portfolio growth between 2002 and 2012. The government supported the buildup of assets through K477 million of debt write-downs and equity injections, and by allowing SOEs to reinvest the majority of their earnings rather than pay dividends.

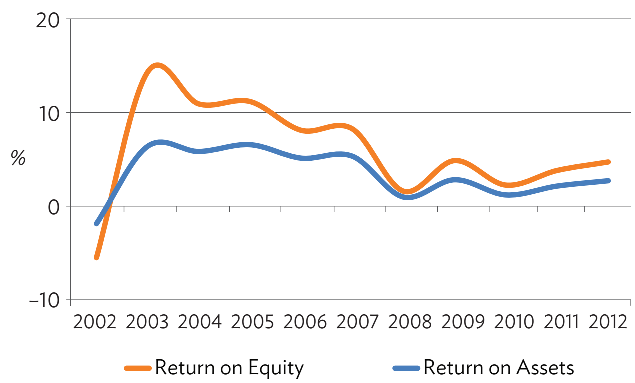
Figure 21: Papua New Guinea State-Owned Enterprise Portfolio Assets, FY2012 (K6 billion)



FY = financial year, K = kina, PNG = Papua New Guinea.
Source: Independent Public Business Corporation.

33 SOEs are currently signing management contracts that may serve a similar purpose as SCIs.

Figure 22: Papua New Guinea State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



FY = financial year.
Source: Independent Public Business Corporation.

Recent government moves have enlarged SOEs' role in natural resource developments, potentially transforming the portfolio's size and composition. In 2013, the government nationalized Ok Tedi Mining Limited—making it PNG's newest SOE. While the company has been valued at up to $2 billion, its nationalization is subject to legal challenge. The Government also re-incorporated the National Petroleum Company of PNG as an SOE, mandated to manage the State's $2.9 billion equity in the PNG liquefied natural gas project.[34]

Regulatory contracts for monopoly service providers have helped to ensure strong revenue growth, but have not produced expected efficiency gains. PNG's Independent Consumer and Competition Commission regulates five SOEs as monopoly service providers. Regulatory contracts (of up to 10 years) establish a price path tied to agreed performance standards and investment plans. Those regulatory contracts without productivity clauses have allowed some SOEs to increase prices above the inflation rate, to generate profits to finance their investment plans. Frustration at the slow rate of improvement in SOE services has encouraged changes in market regulation, including enhanced monitoring of SOE performance and increased private sector participation.

Low interest rates can mask poor performance by inflating the return on equity. Historically, cheap credit added as much as 4.7% to SOE equity returns, but in 2012 this had fallen to less than 0.3% as the spread between SOE borrowing costs and commercial interest rates narrowed. The Department of Treasury has developed a policy to govern on-lending practices, to ensure SOEs borrow at market rates. This will maintain the pressure on SOEs to invest efficiently, and support competitive neutrality between SOEs and private companies that do, or may, compete.

Box 5: Community Service Obligations and Competitive Neutrality

In 2013, the government established the People's Microbank (PMB) as a wholly owned subsidiary of the National Development Bank. PMB competes directly with private banks and microbanks for market share.

While PMB's mandate is to expand access to financial services, a similar, less-costly outcome could have been achieved by inviting private banks to bid for the lowest subsidy required to reach a specified number of new customers.

The existence of PMB—with its community service obligation mandate—undermines competitive neutrality.

The government has moved to promote competition in the power and telecommunications sectors, but risks undermining competition in the banking sector. In 2011, the National Executive Council endorsed the Electricity Industry Policy. The policy supports greater private sector participation in power generation, as a key enabler of service improvements and efficiency gains. In 2013, PNG Power was directed to contract with private power suppliers rather than develop new capacity on its own. In the telecommunications sector, the government has established a new SOE (PNG DataCo) to own the government-funded national fiber-optic network. This is to be available on an open-access basis.

Concurrently, the government instructed the National Development Bank (NDB) to reduce its lending rate to 6.5% to stimulate competition. This direction, and the establishment of the People's Microbank, could harm competition by undermining private banks' sustainability (Box 5).

A new CSO policy should help support greater commercialization of the SOEs, but the benefits will be greatest if private companies are allowed to bid for CSOs. The majority of SOEs provide CSOs, mostly funded through cross-subsidies. They are criticized for providing weak incentives for service provision in high cost areas, preventing more efficient providers from entering the market, and undermining SOEs' focus on commercial performance. The CSO policy follows international best practice and, when implemented in 2014, will help to improve outcomes for SOEs, consumers, and the government.

[34] These changes are not reflected in the portfolio size or performance reported in this study, as they occurred after the end of the 2012 financial year.

Greater use of PPPs could help improve SOE efficiency and profitability. If credible partners are chosen, and the contracting framework is robust, PPPs can help SOEs to operate more efficiently. PNG has a PPP policy and plans to pass legislation in 2014. This could herald greater use of PPPs, such as the operating concession for Eda Ranu's water supply assets in Port Moresby—a well-managed utility that generated an average ROE of 12% from FY2010–FY2012.

Corporatization has not prevented political interference in SOEs' operations. While the government recognizes the benefits of corporatization and commercialization, undue political intervention in SOE management and operations undermines performance. Recent moves to replace Telikom's chief executive officer (CEO), direct the NDB to reduce its interest rates, and overturn an increase in electricity prices approved by the regulator undermine the SOEs' commercial mandate and independence. Decisions motivated by short-term political gain result in long-term value destruction.

Deficiencies in the current legal and governance framework and problems with compliance have contributed to SOEs' poor commercial performance. PNG's SOE portfolio is held in the General Business Trust (GBT) managed by the Independent Public Business Corporation (IPBC),[35] which performs a dual role of trustee and SOE monitor. Amendments to the IPBC Act in 2012 reversed previous changes that had weakened the legal framework. Notable deficiencies remain, however, including the absence of an explicit commercial objective for SOEs. Noncompliance with key elements of the Act has been a problem since 2002, leading to weak governance and accountability. The IPBC has consistently failed to publish annual reports with audited financial statements for the IPBC, GBT, and individual SOEs. Greater transparency would strengthen the performance incentives for the SOEs. Certainly, low levels of transparency have contributed to their poor performance.

Plans for overhauling the legal and governance framework for SOEs are progressing but the policy principles guiding this change remain unclear. In 2012, the government convened two major SOE forums to consult stakeholders on the key principles for a new SOE policy framework. Under the proposed new framework, the SOE portfolio would be transferred into a new holding company owned by a specially created trust. Trusts lack transparency and suffer from confused accountabilities. A clear policy that embeds best practice principles on SOE governance and monitoring, and upholds competitive neutrality, would drive improved performance more effectively than fine-tuning the ownership structure.

[35] Established by the Independent Public Business Corporation Act 2002.

G. SAMOA

Samoa was once regarded as an aggressive SOE reformer in the Pacific, but the pace of reform has slowed. Since the mid-1980s, half of its SOEs have been restructured. During 2001–2004, the government adopted international accounting standards, enacted a new SOE law,[36] and approved the SOE Ownership, Performance, and Divestment Policy advocating the divestment of all nonstrategic SOEs.[37] The government has reconfirmed this policy in successive publications of its key planning document, the Strategy for the Development of Samoa (SDS).[38] However, there have only been two privatizations since 2007—SamoaTel and Samoa Broadcasting Corporation (Box 9). The 2012–2016 update of the SDS lacks any substantive SOE reform targets.

Table 10: Samoa Key Indicators

Population (total), 2012	188,889
GDP (current $), 2012	683,719,606
GDP per capita (current $), 2012	3,620
Population density (persons per km^2), 2012	67
Total surface area (km^2)	2,944
Number of islands	9
Number of SOEs included in this study	17

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

There have been no significant variations in individual SOE performance over recent years. Two historically profitable SOEs, Samoa Shipping Corporation and Polynesian Airlines, have seen a sharp decrease in profitability since 2010, but the balance of the portfolio has generally been stable. The 5 largest SOEs represent 71% of the total assets, but only 6 of the 15 SOEs generated a profit in 2012.

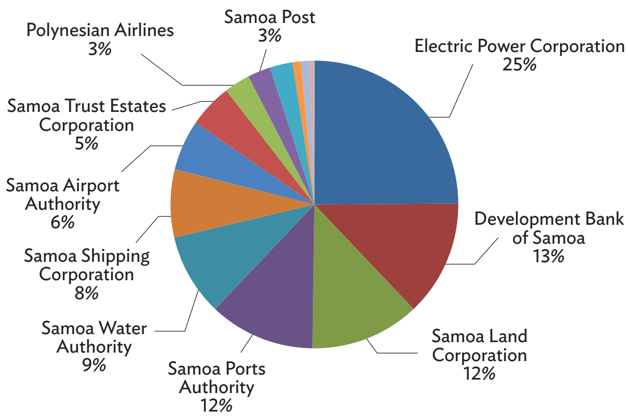
The SOE portfolio continues to perform well below the government's target of 7% ROE. Average ROE and ROA for FY2002–FY2012 was 0.1%. Samoa is one of only three countries in the benchmarking sample to show no material improvement in portfolio ROE for FY2002–FY2012, despite access to subsidized credit—7% below the commercial rate on average—and an estimated $134 million in government transfers.

[36] The Public Bodies (Performance and Accountability) Act 2001.

[37] The SOEs considered strategic included Electric Power Corporation, Samoa Airport Authority, Samoa Ports Authority, Samoa Shipping Corporation, and Samoa Water Authority.

[38] Strategy for the Development of Samoa, 2008–2012.

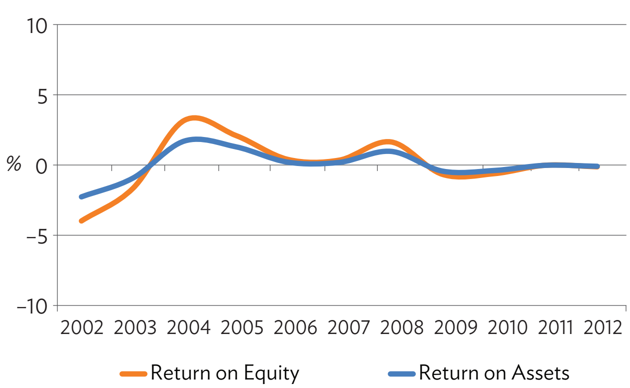
Figure 23: Samoa State-Owned Enterprise Portfolio Assets, FY2012 (ST1 billion)



FY = financial year, ST = tala.
Source: State-Owned Enterprise Monitoring Unit, Ministry of Finance.

Government transfers to SOEs during 2002–2012 were equivalent to 2.6% of GDP averaged over the period. This contrasts sharply with Tonga, where the SOEs made a $14 million net contribution to government. The social and economic cost of subsidizing underperforming SOEs is significant—government transfers equate to 53% of the total spending on health. The government continues to support loss-making (and insolvent) SOEs through soft loans, or investments directed through Samoa National Provident Fund, Development Bank of Samoa, or the Accident Compensation Corporation.

Figure 24: Samoa State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



FY = financial year.
Source: State-Owned Enterprise Monitoring Unit, Ministry of Finance.

Since 2011, the Unit Trust of Samoa (UTOS) has become a major source of subsidized SOE loans. To generate revenues to meet its overhead costs, UTOS has embarked on an aggressive financial disintermediation program, raising funds from the public and local institutions and lending the money to SOEs at below commercial rates. The government guarantees the loans to the SOEs. UTOS is not only crowding out lending to the SOEs by commercial banks but, by providing subsidized loans to SOEs, it also gives the SOEs a competitive advantage. Provision of subsidized loans may encourage SOEs to undertake

Box 6: Unit Trust of Samoa

The Unit Trust of Samoa (UTOS), established in 2010 under the Prime Minister's sponsorship, was intended as a vehicle for ordinary Samoans to participate in state-owned enterprise (SOE) privatizations. The Trust's first investment was 25% of the privatized SamoaTel, funded by a ST7.9 million government loan. While its prospectus identifies other SOEs as potential investments, no further privatizations have been completed.

To meet its ST500,000 annual operating costs, UTOS has been forced to seek alternative investments. By the end of FY2013, UTOS issued ST11.2 million of units to investors and borrowed ST41.0 million from Accident Compensation Corporation, Samoa National Provident Fund, Samoa International Finance Authority, Parliamentary pension scheme, and other SOEs—all controlled by the government—and lent ST52.4 million to various SOEs and government-owned commercial businesses. UTOS' liabilities are generally long term, while its loans are short term, resulting in a significant maturity and interest rate mismatch.

UTOS distorts the market and SOE behavior as follows:

- It unfairly competes against the commercial banks.
- It influences interest rates and commercial banking sector liquidity.
- Loans to SOEs are covered by a free government guarantee—normally the government charges SOEs for guarantees.
- SOEs do not need to meet commercial credit criteria.
- UTOS profits are tax free.
- The government guarantees for the SOE loans and returns from the SamoaTel investment represent a fiscal risk for the government.
- Taxpayers are effectively funding distributions to unit holders.
- SOEs receive "cheap" money, and may be tempted to invest poorly.

FY = financial year, ST = tala.

or continue noncommercial investments. By June 2013, the UTOS had ST52 million in outstanding loans to SOEs and government-owned commercial businesses.[39]

Important steps have been taken to strengthen SOE governance, but ministers continue to exercise undue influence over board decisions. The 2010 establishment of an independent director selection panel and passage of the Composition Act in 2012 resulted in all ministers resigning from SOE boards, and 180 new director appointments. While the SOE Act prohibits nondirectors from influencing board decisions, ministers and Cabinet have historically had significant operational control over the SOEs.[40] The recent reforms should lessen direct ministerial control over SOE board deliberations and make Cabinet directions more transparent, yet early indications are that ministers— individually and collectively through Cabinet—continue to intervene in SOE matters. This is contrary to the SOE law.

Samoa has a robust legal, governance, and monitoring framework for SOEs, but it has never been fully implemented. As has been demonstrated in Solomon Islands, SOE performance would improve if the government fully implemented its SOE Act. This should be supported by publishing SOE accounts and achievements against key performance targets. Increased disclosure would allow increased stakeholder engagement and scrutiny of SOE performance and commercial returns.

Box 7: Inappropriate Ministerial Interference

There are numerous examples of inappropriate ministerial influence, both pre- and post-passage of the Composition Bill.

Cabinet was active in supporting—if not driving—a series of noncommercial investments by the Samoa Ports Authority. The resulting ST24 million debt burden, combined with the poor profitability of the investments, drove the company toward insolvency. It was rescued with a ST63 million government transfer in 2012.

In March 2010, Cabinet directed the Agricultural Stores Corporation to transfer land valued at ST2.7 million to another state-owned enterprise (SOE), for a consideration of ST0.80.

In 2012, the Samoa Airport Authority was directed by the responsible minister to discount the rent charged to a private sector tenant for a large section of airport land.

ST = tala.

[39] ST54 million includes a loan of ST16.5 million to the government-owned Pacific Forum Line.

[40] The Act stipulates that directors are solely responsible for SOE performance and imposes financial penalties if nondirectors, including ministers, seek to unduly influence the independent board process.

The government recently appointed an SOE Minister responsible for all SOEs. The Minister of Finance will focus on the fiscal oversight of SOEs, including their impact on the government's financial position. The SOE Minister will focus on the ownership interest: governance, the return on investment, long-term organizational health, and effective financial and operational monitoring. This very positive development should improve monitoring effectiveness.

H. SOLOMON ISLANDS

The Solomon Islands SOE portfolio has undergone a dramatic turnaround since 2008. It is now the most profitable portfolio in the Pacific, and in the benchmarking sample. Average ROE of the portfolio increased from –12% in FY2002–FY2008, to 6% for 2009–2012 and 15% in FY2012. The turnaround can be attributed to four factors:

- Financial restructuring of three major SOEs: Solomon Airlines Limited (SAL), Solomon Islands Electricity Authority (SIEA), and Solomon Islands Water Authority (SIWA);
- Tariff increases for SIWA and Solomon Islands Port Authority (SIPA), and improved collections for SIEA and SIWA;
- Improved implementation of the SOE Act, particularly the CSO regulations; and
- Privatization/liquidation of nonstrategic SOEs.

The portfolio is relatively small, with only 6 active SOEs, 3 of which represented 90% of the assets and 100% of the profit in 2012. The financial restructuring of three of the four largest SOEs has cost the government an estimated SI$21 million since 2011, involving the settlement of arrears,

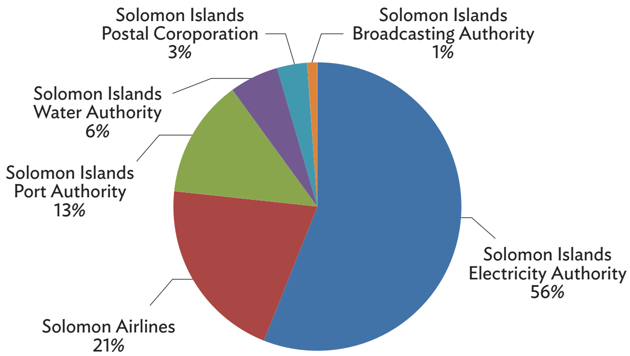
Table 11: Solomon Islands Key Indicators

Population (total), 2012	549,598
GDP (current $), 2012	1,008,424,232
GDP per capita (current $), 2012	1,835
Population density (persons per km^2), 2012	20
Total surface area (km^2)	28,900
Number of islands	1,000
Number of SOEs included in this study	11

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.

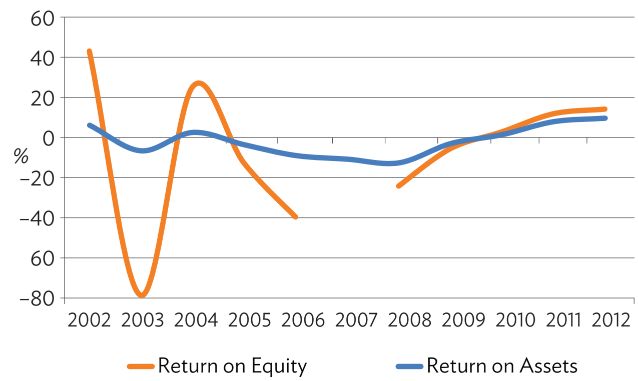
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Figure 25: Solomon Islands State-Owned Enterprise Portfolio Assets, FY2012 (SI920 million)



FY = financial year, SI$ = Solomon Islands dollar.
Source: Ministry of Finance and Treasury.

Figure 26: Solomon Islands State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012[a]



[a] Portfolio equity was negative in 2007.
Source: Ministry of Finance and Treasury.

debt forgiveness, and new equity investment.[41] In contrast to previous restructuring efforts, the financial assistance has been accompanied by measures to place the SOEs on a more sustainable, commercial footing. SIEA has substantially improved metering and collections, while SIWA has increased tariffs to approach cost-recovery levels and is now focusing on reducing nonrevenue water.

The smaller SOEs continue to struggle, and need substantial restructuring. Solomon Islands Broadcasting Corporation (SIBC) and Solomon Islands Postal Corporation (SIPC) have reduced operating costs and increased revenues, but it is unclear if these efforts will ensure sustainability. In both cases, selected activities could be discontinued, contracted out, or sold to the private sector to attract new investment and expertise for both businesses.

All SOEs are undercapitalized, and need partnerships with the private sector to survive. Most SOEs are looking to make substantial capital investments over the next 5 years. SIEA, SIPA, and SAL could finance a portion of these investments from internal resources and/or borrow from commercial lenders. The government's borrowing limits are restricting SOE financing. PPPs, outsourcing, and privatization could address SOE capitalization requirements. A new policy on SOE ownership, divestiture, and PPPs is needed to guide the SOE restructuring program.

The government has successfully divested profitable and unprofitable SOEs. Since 2008, four SOEs have been divested using different mechanisms; a PPP (Sasape Marina: see Box 13); a merger with the Solomon Islands National Provident Fund and Home Finance Limited; a sale of shares to existing private shareholders (Soltai); and a liquidation of assets (SolPrint). All four transactions resulted in a reduced fiscal burden on the government; two have catalyzed new investment from the private sector, and an expansion of service opportunities. This experience demonstrates that privatization can be successful, even for loss-making SOEs.

The portfolio's strong recovery remains fragile, and depends on the government's continued implementation of the SOE Act. The Act and its supporting regulations[42] establish a robust framework for commercially managing SOEs. It requires the SOEs to operate profitably; imposes a rigorous director selection and appointment process; defines corporate planning and reporting requirements; and establishes a process for the transparent identification, costing, and financing of CSOs. A monitoring unit[43] within the Ministry of Finance and Treasury provides oversight, reporting to accountable ministers on SOE performance. Even with donor support, the unit has struggled to fulfill its mandate. Undertaking its role effectively requires more specialized professional staff and further capacity development.

[41] SIEA and SIWA were also granted exemptions from import duties and taxes for 2 years. These would have amounted to approximately SI$39 million.

[42] The State-Owned Enterprise Act 2007 and State-Owned Enterprise Regulations 2010.

[43] Economic Reform Unit.

The CSO process has been successfully integrated into the budget, with five CSO contracts signed in 2013. These performance-based contracts trigger payments after services are delivered. Through the contracts, the government is now able to assess the cost of the CSOs, and make choices based on the benefits generated. In 2013 and 2014, SI$21 million and SI$39 million were approved to finance the CSOs, respectively.

Corporate planning and reporting remain weak. With the exception of the largest SOEs, others struggle to prepare meaningful statements of corporate objectives (SCO) and corporate plans, or submit their audited annual accounts within 3 months of a financial year.[44] In 2013, all SOEs prepared SCOs, but most did not prepare business plans and only SIEA completed its audited annual accounts within the required time. Following the preparation of SCO guidelines the process is improving, but the smaller SOEs require continued support from the Ministry of Finance and Treasury and donors to comply with the Act's planning and reporting requirements.

Violations of the SOE Act still occur, but are increasingly rare. The attempt to reappoint the former CEO of SIPA in September 2013, contrary to the provisions of the SOE Act, is a recent example. The attempted reappointment—opposed by the board—resulted in a 6-month impasse, impacting a vital economic resource. The episode illustrates that, while violations of the SOE Act can still occur, the Act is becoming better understood and is serving as an effective deterrent to ministerial intervention into the affairs of SOEs.

Maintaining reform momentum will require strong political will and increased stakeholder involvement. When political resolve to enforce the SOE Act weakens, civil society, the public, and other stakeholders can pressure politicians to comply with the law. This requires effective information dissemination, including the laws' broad provisions, the directors' roles and responsibilities, how elected officials can properly direct an SOE's affairs, and the consequences of poor SOE performance. In Solomon Islands, this could be achieved by publishing SOE accounts (as the SOE Act requires), holding public information campaigns explaining the SOE roles, and conducting training for SOE directors.

I. TONGA

Tonga continues to pursue a broad-based SOE reform program that began in 2002. The pace of reform increased significantly after 2006 and much was achieved through to 2010, including privatizing 2 SOEs, developing restructuring plans for 10 SOEs, and amending the SOE Act. The amendments require SOEs to operate profitably; prohibit the appointment of elected officials to SOE boards;[45] and strengthen corporate planning, disclosure, and CSO processes. Tonga is the only Pacific island country that publishes summaries of SOE audited annual accounts in local newspapers, with performance against targets set in the business plan.

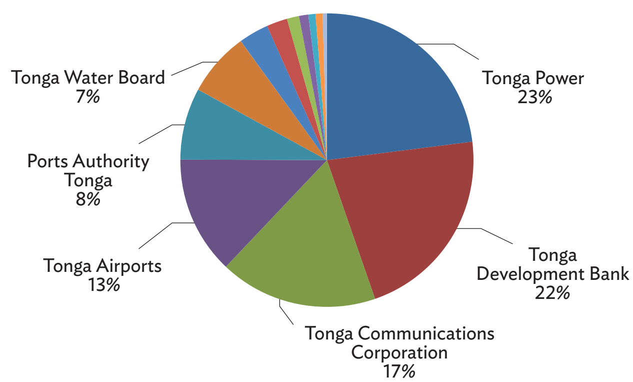
The 2010 amendment to the SOE Act led to restructured SOE boards, with independent directors replacing ministers and boards held more accountable for the performance of their SOE. Despite these reforms, the portfolio's overall profitability deteriorated through 2011 and 2012. This mainly reflected the dramatic decline in Tonga Communications Corporation's (TCC) financial performance, which generated 48% of the portfolio's

Table 12: Tonga Key Indicators

Population (total), 2012	104,941
GDP (current $), 2012	471,575,497
GDP per capita (current $), 2012	4,494
Population density (persons per km^2), 2012	146
Total surface area (km^2)	748
Number of islands	176
Number of SOEs included in this study	18

GDP = gross domestic product, km^2 = square kilometer, SOE = state-owned enterprise.
Sources: World Bank. World Development Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=world-development-indicators; World Health Organization; and Department of Foreign Affairs and Trade (Australia).

Figure 27: Tonga State-Owned Enterprise Portfolio Assets, FY2012 (T$284 million)

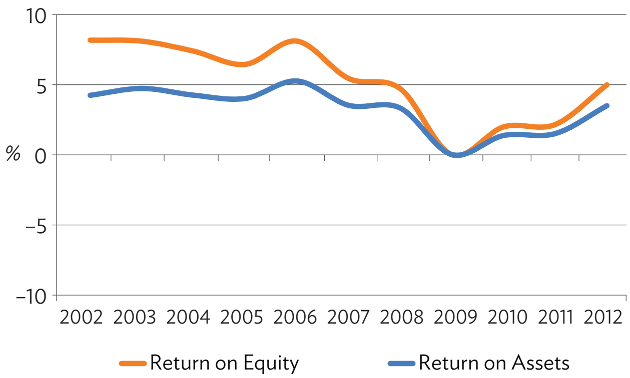


FY = financial year, T$ = pa'anga.
Source: Ministry of Public Enterprises.

[44] Section 14 of the State-Owned Enterprise Act 2007.

[45] Except for newly established SOEs, where elected officials can be appointed for the first 12 months following establishment.

Figure 28: Tonga State-Owned Enterprise Portfolio Return on Equity and Return on Assets, FY2002–FY2012



Source: Ministry of Public Enterprises.

total profits in FY2002–FY2012 but made a loss in 2011, as the SOE struggled to deal with strengthened competition.

The portfolio recorded a modest 5.2% average ROE and 3.2% average ROA for FY2002–FY2012. While this is the third highest average ROE in this benchmarking sample, it is well below the government's 10% ROE target and the return required to compensate the government for the portfolio's risk-adjusted cost of capital. Six of the 13 SOEs account for 90% of total assets and drive the portfolio returns. Only Tonga Power and Tonga Development Bank (the SOEs with the most commercially driven and independent boards) posted ROEs in excess of 5% in FY2012.

The government appears reluctant to hold directors accountable for performance, which may be explained by family connections and the closeness of Tongan society. If the government is determined to achieve better SOE performance—financial and operational—it must manage such conflicts of interest, only appoint directors on merit, and hold them accountable for performance.

Donor-funded budget support programs with SOE reform conditions have provided much-needed impetus. The amendments to the SOE Act and associated reforms were conditions under a 2010 ADB budget support grant. Further reforms have also been framed by budget support programs, which led to the following achievements in 2012–2013:

- liquidation of Tonga Investments, including the sale of its subsidiary Home Gas;
- partial liquidation of Tonga Print;
- 100% compliance with the CSO policy, with six CSO contracts awarded—two to private sector operators;
- creation of a skills-based selection and appointment process for all SOE directors;
- implementation of a director performance evaluation system in all SOEs;
- Cabinet approval for restructuring TCC, including possible privatization; and
- 60% of all SOE audited accounts made current, with a target of 80% by FY2014.

Despite these achievements and Tonga's weak fiscal position, Cabinet appears reluctant to push reform to the next level. Reform remains fragile as ministers struggle with the formal separation of roles between the board and political oversight. Some ministers have sought to reverse the prohibition on being appointed as SOE directors, and others have attempted to set prices charged by monopoly SOEs in contravention of the CSO requirements in the SOE law. However, conditions linked to donor funding disbursement have ensured that ministers abide by the legislation. The strengthened SOE Act provides ministers with effective oversight—they have only to use the existing provisions. That also means that their actions would be transparent and accountable.

Tonga is in an enviable position—its legislative, governance, and monitoring frameworks are robust. A new Minister of SOEs has moved to strengthen the ownership monitoring function within the ministry and build capacity within the SOE boards. Restructuring strategies already exist for a number of SOEs, and the Minister has set an ambitious reform program that will include some of the largest SOEs.[46] If implemented, the portfolio should move closer to the government's 10% ROE target and generate much-needed cash. To be successful, the program will require broader political commitment, including from Cabinet.

[46] Ports Authority Tonga, TCC, Tonga Airports, Tonga Development Bank, Tonga Water Board, and Waste Authority.

IV. CHALLENGES OF STATE-OWNED ENTERPRISE REFORM

A. HAS STATE-OWNED ENTERPRISE REFORM SUCCEEDED GLOBALLY?

State-owned enterprise (SOE) reform has been central to broader economic restructuring programs throughout the world, starting in Chile, New Zealand, and the United Kingdom in the 1980s. All programs aimed to improve performance by placing SOEs on a more commercial footing.[47] When countries experienced macroeconomic imbalances, the budget drain from SOEs became difficult to sustain. Many countries therefore initiated reform programs that ranged from attempting to commercialize SOEs, to outright privatization.

The evidence consistently shows that, despite repeated attempts at reform, endeavoring to impose commercial discipline on SOEs has rarely yielded satisfactory results over a sustained period. SOEs continue to underperform compared with the private sector, and often cannot operate without some government support. Even when strong commercial requirements were imposed on SOEs, after an initial period when productivity and profitability improved, the SOE portfolio performance steadily declined over time.

Box 8: Hero to Zero in 3 Years—New Zealand's Solid Energy

Solid Energy aggressively expanded from early 2000, encouraged by its owner, the Government of New Zealand. The Board estimated the company's value at NZ$3.5 billion in 2010.

By early 2013, the realizable value of the company's assets was less than its NZ$390 million debt and it was facing liquidation—laying off more than 25% of its workforce.

What went wrong? The company expanded while coal prices fell by 40%; staff received bonuses while earnings dropped by 146%. The board failed to question management, and then refused to provide information to its shareholder—the government.

The failure of Solid Energy demonstrates the state-owned enterprise model's inherent weaknesses. Commercial risk is often underpriced, board and management behave as owners, and governments struggle to respond quickly to changed commercial, governance, or market conditions.

NZ$ = New Zealand dollar.

Reporting on Australian SOE performance in 2002, the Australian Government Productivity Commission stated: "Despite the intent of governments to operate SOEs on a commercial basis, over 60% of monitored SOEs earned less than the long-term bond rate in 2001–2002. An even greater number of SOEs failed to earn a commercial rate of return, when a margin for risk is included."[48] In New Zealand, where SOEs initially dramatically improved their profitability after the reform program launched in 1984, the gains proved unsustainable. Reforms led to an average portfolio return on equity (ROE) of 8.7% by 2000, but performance steadily declined thereafter, with average ROE falling to 7.9% in 2000–2005 and to 4.3% in 2005–2010.[49] In 2012 and 2013, the outcomes were even bleaker with the weighted average ROE registering a negative 17.4% in 2012 and just 0.1% in 2013.[50]

Poor SOE performance is the norm for most countries. Government ownership provides weak incentives for efficiency, strong incentives for political accommodation at the expense of commercial outcomes, and political pressures to overstaff and undermaintain. Over time, many governments view SOEs not as commercial ventures but as political liabilities. SOEs are managed to reduce political risks, not optimize commercial returns and operational efficiency.

This is the fundamental flaw in the SOE model: politicians always find difficulty with commercial decisions that have political costs. These costs include job losses, closing down loss-making businesses, or disallowing power and water utilities from charging true service costs. Politicians often see SOEs as entities that can accrue political patronage through providing community services without adequate compensation, or vehicles to employ their supporters. Rare is the government

47 Restructuring programs were usually associated with broader macroeconomic policy reform because SOEs frequently drained government budgets. For example, Jamaica—one of the most heavily indebted countries in the world—recently divested Air Jamaica, which was requiring budget support equivalent to nearly 2% of GDP.

48 Productivity Commission. 2003. *Financial Performance of Government Trading Enterprises, 1997–98 to 2001–02*. Commission Research Paper. AusInfo: Canberra.

49 Source: New Zealand Treasury. Significant railway assets acquired from Ontrack were added to the SOE portfolio, which had a negative impact on returns for FY2007 and FY2008. The impact of Ontrack has not been discounted from these numbers, because it was a government decision to reacquire the assets and add them to the SOE portfolio.

50 The New Zealand government has recently reclassified its state-owned companies, combining the SOEs with other commercial state-owned companies to form a group labeled the "Commercial Priority Portfolio." This has not materially changed the portfolio's consolidated financial performance.

Box 9: Samoa Broadcasting Corporation Demonstrates Quick Wins from Privatization

In 2008, the Government of Samoa privatized the Samoa Broadcasting Corporation, which operated AM/FM radio and a television (TV) station competing with private sector providers. Despite a history of profitability, the company recorded losses and a negative return on equity in 2006 and 2007, the years preceding the sale.

The company was offered for sale by competitive tender, which was awarded to a consortium led by the company's management. Four major shareholders (including the presale chief executive officer) now own 90% of the company's equity, with staff holding the balance. The government opted to retain the AM channel for public announcements and public emergency broadcasts.

A little over 1 year after the sale, the new owners reported improvements in almost all aspects. In the first year after acquisition, the company profited sufficiently to pay the new owners a dividend. In the second year, the directors elected to retain the profits in the business for reinvestment.

Radio coverage has increased from 85% of the population to 98%, and TV broadcasting hours have been extended. The company has expanded its TV program offering and invested an estimated ST400,000 in broadcasting infrastructure. Staff morale and commitment have improved.

This sale demonstrates that privatization can bring immediate operating benefits and improved profitability, and also that state-owned enterprises can be sold for fair value even when making losses. Purchasers will value a business based on how they will manage it and the business opportunities they can identify, not on the success or failure of the previous owners' business strategies.

ST = tala.

that will agree to allow necessary price increases for SOE outputs when elections are pending. Because of these inherent challenges to state ownership, the SOE model was never designed as a long-term ownership model, but as a vehicle to transition from state to private control.

B. CHANGING HOW THE STATE SUPPLIES GOODS AND SERVICES: PRIVATIZATION AND PUBLIC–PRIVATE PARTNERSHIPS

The alternative to continued government ownership is privatization, which international experience demonstrates results in more efficient public service provision than state ownership. Privatization is the most effective means of locking in efficiency gains created by restructuring government departments into SOEs and ensuring further improvements in operational performance.

Some argue that SOEs "belong to the people" and that selling them would be against the public interest. Public welfare is not determined by who owns SOE assets, but rather who benefits from the capital, plant, and machinery SOEs use. If assets under SOEs are used less productively than under private ownership, "the people" will benefit far more from their sale to private sector operators that can provide the services more efficiently.

From the mid-1980s to the mid-2000s, SOEs valued at almost $1 trillion in total were privatized in more than 100 countries. The bulk of privatizations occurred in the 1990s. Early adopters of large-scale privatization programs were Canada, Germany, Mexico, New Zealand, and the United Kingdom. By the mid-1990s other regions had followed, most notably Eastern Europe and Latin America. Boxes 9, 11, and 13 outline examples of privatizations markedly improving the performance of formerly state-controlled assets and, in so doing, benefiting government budgets and user groups.

Private ownership brought much-needed commercial discipline, capital, and expertise, as well as access to new markets. When transactions failed, they were usually poorly prepared or lacked regulatory frameworks to ensure that public monopolies did not become abusive private monopolies. A study on the performance of SOEs privatized through public listing in New Zealand and Australia found that, in New Zealand, after a 2-year holding period, the privatized portfolio had on average realized an 18.1% annualized return compared with the market index return of 8.1%. In Australia, the returns for a comparable period were 39.6% and 13.8%, respectively.[51]

Privatization's economy-wide effects on government budget, growth, employment, and investment are also positive. Another study involving 18 countries with significant privatization programs reported substantial budget inflows from privatization, accounting for nearly 2% of annual gross domestic product.[52] Although there were some short-term job losses as a result of privatization transactions, they were often offset by longer-term growth in the economies where the privatizations occurred.

[51] J. Kerr, M. Qiu, and L.C. Rose. 2008. Privatisation in New Zealand and Australia: An empirical analysis. *Managerial Finance*. 34(1). pp. 41–52.

[52] N. Birdsall and J. Nellis. 2002. Winners and Losers: Assessing the Distributional Impact of Privatization. *Working Paper No. 6*. Washington, DC: Center for Global Development.

Box 10: Studies Demonstrate the Benefits of Private Ownership

Many international studies have shown that state-owned enterprises (SOEs) perform less well than private sector companies. For example, a 2004 study by the Norwegian Institute of International Affairs concluded "using return on assets as the measure of performance and carefully controlling for market structure and a range of factors that may have an impact on company performance; we find that the performance of SOEs is indeed inferior to that of private companies."[a] The same study also concluded that SOEs perform badly even where they have a favorable market structure and little competition.

Empirical evidence demonstrates that privatization improves business efficiency, boosts market competitiveness, and increases overall economic welfare. In a 2004 survey, 20 out of 22 academic studies on the effects of privatization observed that businesses performed better after privatization. Ten of the studies compared the performance of public and private enterprises operating in the same industry; eight concluded that privately owned enterprises performed better.[b] The survey also found that privatization increased the competitiveness of the markets in which former SOEs operated, as previously state-subsidized or state-favored businesses were forced to succeed (or fail) on their own.

Three surveys by the Organisation for Economic Co-operation and Development (OECD)[c] and the World Bank[d] contain similar findings. These surveys, which reviewed over 50 published empirical studies examining hundreds of privatization transactions, showed that

(i) private firms tend to be more efficient than their state-owned counterparts; and

(ii) privatized SOEs usually lead to a more efficient enterprise and a more open and competitive market (benefiting consumers, taxpayers, and the whole economy).

The evidence does not show that private ownership is always more efficient. What it does show is that—on average and over time—the private sector is likely to run commercial enterprises more efficiently than the public sector.

[a] E. Goldeng, L.A. Grünfeld and G.R.G. Benito. 2004. The Inferior Performance of State-Owned Enterprises: Is it Due to Ownership or Market Structure? *NUPI Working Paper No. 663*. Oslo: Norwegian Institute of International Affairs.

[b] P. Barry. 2004. Does Privatisation Work? Policy Backgrounder No. 5. Wellington: New Zealand Business Roundtable. December.

[c] R. Gönenç, M. Maher, and G. Nicoletti. 2000. The Implementation and the Effects of Regulatory Reform: Past Experience and Current Issues. *OECD Economics Department Working Papers No. 251*. Paris: OECD Publishing. http://dx.doi.org/10.1787/413754754615.

[d] M. Shirley and P. Walsh. 2000. Public versus Private Ownership: The Current State of the Debate. *Policy Research Working Paper No. 2420*. Washington, DC: World Bank.

Even partial privatization in the countries in our study produced better results than 100% state ownership. All evidence suggests that Pacific island countries that do not privatize their SOEs are forgoing major growth opportunities. Infrastructure SOEs—where they are monopoly providers—may be better suited for partial privatization or public–private partnerships (PPPs). Community service obligations (CSOs), often found in infrastructure SOEs, can continue to be provided under private ownership, as demonstrated in Fiji and Tonga.

Privatization and PPPs create market and investment opportunities for the private sector. By contracting out selected services, SOEs can enable smaller local firms to bid for the new services, either on their own or in joint venture with offshore parties. While it is often believed that privatization results in the sale of important state assets to foreign investors, 12 out of 16 full or partial divestitures of SOEs in the Pacific since 1998[53] were acquired by domestic investors. In Jamaica, local interests have invested in 14 of the 22 SOEs fully or partially privatized since 1999.

The experiences of all the countries participating in this study demonstrate that privatization transactions are successful when properly prepared. Proper preparation includes prequalifying bidders, providing for potential employee redundancies, and introducing competitive tension in the sales process. Where privatization involves an effective or natural monopoly, regulatory frameworks must adequately protect consumers' interests.

When full privatization is not politically feasible, partial privatization can help accelerate commercialization and improve SOE performance. One of the most common forms of partial privatization is the joint venture, where the public and private sectors collaborate in forming a company to provide specific services. The partial privatization of Polynesian Airlines in Samoa produced dramatic and sustained improvements in service and efficiency, benefiting consumers and local tourism (Box 11).

In countries with established stock exchanges, partial privatization can also be achieved through public listing. This is a common practice throughout the world and offers the dual benefit of (i) introducing greater commercial incentives in SOEs, while also (ii) supporting capital market development. Although the efficiency gains resulting from partial privatization are generally weaker than for full privatization, the performance of partially privatized entities generally improves because minority shareholders demand better results, thereby reducing the need for public sector monitoring. Studies show that "the

[53] Ten transactions in Samoa; and two each in Fiji, Solomon Islands, and Tonga.

Box 11: Successful Partial Privatization in Samoa—Polynesian Blue

In Samoa, Polynesian Airlines was imposing substantial costs on the economy. In FY2001–FY2002 it required an infusion of ST20 million from the government to keep running. These funds were provided by cutting spending on health and education. A joint venture was entered with Virgin Australia that resulted in the formation of Polynesian Blue; the government and Virgin each owning 49% of the shares, with the remaining 2% owned by a Samoan business. This has resulted in eliminated budget drain, lower airfares, and increased tourism.

ST = tala.

possibility of shareholders exerting both voice and exit may lead to higher profitability in [mixed enterprises] compared to 100% state-owned enterprises."[54] However, a study on the performance of Brazilian SOEs partially privatized and listed in 1976–2009 noted that, while the transformation from state owner and manager to majority shareholder has reduced many agency problems, it has not reduced government temptations to intervene in the operation of large strategic enterprises.[55]

There is significant value in SOEs in this survey. Substantial cash proceeds could be generated through partial privatizations, and even more through full privatization (Box 12). Fiji is contemplating partial privatization of SOEs through public listing, and Papua New Guinea (PNG) is may follow suit. The potential for these types of operations in the region is significant.

In some cases, PPPs can be more suitable than full privatization for attracting private investment.[56] PPPs have been used extensively throughout the world to improve the quality and coverage of infrastructure services. PPPs create strong performance incentives and allow the public and private sectors to share risks over time. Sometimes they encourage substantial private investment in upgrading core infrastructure. The most common PPPs include the following:

(i) **Service contracts.** The private sector provides a service, such as road maintenance or transport, for a fee.

[54] C. Sam. 2007. Partial privatization, corporate governance, and the role of state-owned holding companies. *Journal of the Asia Pacific Economy*. 13 (1). pp. 63–88. London: Routledge.

[55] M. Pargendler, A. Musacchio, and S.G. Lazzarini. 2013. In Strange Company: The Puzzle of Private Investment in State-Controlled Firms. *Harvard Business School BGIE Unit Working Paper No. 13-071*. Massachusetts. Available at SSRN: http://ssrn.com/abstract=2217627 or http://dx.doi.org/10.2139/ssrn.2217627

[56] A PPP is not a joint venture; it is a shared-risk contract between the public and private sectors to deliver a specific output over a time period.

Box 12: Unlocking Value in State-Owned Enterprises

To get an indicative market value of state-owned enterprises, and the cash proceeds which could be generated through privatization, an earnings multiple methodology can be used.

Adjusting for market and country risk, this methodology reveals that a controlling interest in utilities such as Tonga Power and Fiji Electricity Authority could be valued at 11 times earnings, or $78 million and $492 million, respectively. Similarly, a controlling interest in the Solomon Islands Port Authority, using an earnings multiple of 7.5, would have an indicative value of $52 million. In the telecommunications sector, a controlling interest in Tonga Communications Corporation, using an earnings multiple of 11, would yield an indicative value of $40 million.

(ii) **Management contracts.** The private sector manages, but does not own, public assets.

(iii) **Concessions.** The private sector modernizes public assets to deliver a specific output.

(iv) **Build–own–lease, or build–operate–transfer.** The private sector builds a new asset (such as a hospital or power generation unit). The asset is then leased back to the public sector (e.g., a hospital), or its output (e.g., power) is sold to the public sector or directly to consumers.

Most countries in this study have had positive experience with PPPs, and plan more. Fiji, PNG, Solomon Islands, and Tonga have contracted out subsidized ferry services to private sector providers. Fiji has PPP contracts for electricity generation, and recently contracted out management of the Suva and Lautoka ports. Cabo Verde is developing operating concessions for its seven ports, with the largest port in Praia expected to be the first. PPPs for the airports, energy, and the delivery of social services are also planned. In Mauritius, the government has developed a PPP framework that has been recently strengthened, anticipating PPPs in road infrastructure and renewable energy in 2014. PNG has developed a PPP policy and contracts for water supply, electricity generation, and shipping services. Samoa has successfully contracted out road maintenance services, resulting in 400% increase in productivity, and developed a wastewater treatment facility on a build–operate–transfer basis.

PPPs can generate real benefits, and simple contracts are not costly. Countries should continue exploring PPP opportunities in the SOE portfolio, so that bankable PPP

Box 13: Sasape Marina—A Public–Private Partnership Success Story in Solomon Islands

In early 2007, the Government of Solomon Islands decided to find a private investor and operator for Sasape Marina Limited (SML). Lack of investment and mismanagement had caused the company's financial and operating position to deteriorate, with the value of the government's equity falling from SI$14 million in 1996 to an estimated SI$3 million in 2005—the last year in which financial statements were prepared. By 2008, the company was insolvent and its assets were in disrepair; both of the company's slipways were inoperable.

Without substantial investment, the company faced certain closure. The government, recognizing its limited capacity to invest in and operate the slipway, turned to the private sector. It was decided that a public–private partnership (PPP) would be the best way to achieve the government's objectives and rapidly install a new operator. A competitive tender was successfully conducted in 2010. The winning bidder, a Solomon Islands shipping operator, presented a plan to rehabilitate and expand the slipway. This made it uniquely capable of servicing the large vessel repairs for the Solomon Islands shipping industry, as well as some from neighboring Papua New Guinea.

The private investor partnered with the National Provident Fund to provide the SI$21 million capital to refurbish the facility. Construction was completed in 2012 and the new 520-ton slipway became operational, employing more than 50 previously unemployed local people. The slipway is the major employer for the 1,750 people living on the small island of Tulagi. Cash has started to flow into the local economy, fuelling the reestablishment of the market. With the proceeds from the sale of SML's assets, the Solomon Islands government was able to finance restructuring costs and repay SML's outstanding debts.

This transaction illustrates that

- insolvent state-owned enterprises (SOEs) can be attractive candidates for PPP or sale,
- pre-transaction restructuring is not required for a successful outcome,
- local investors are ready and capable of injecting new capital to revitalize state assets, and
- private investment ultimately leads to employment creation as assets are used more productively.

This transaction has provided the Solomon Islands government with a solid example of the benefits of PPPs, and the political capital to prepare more SOEs for restructuring or sale.

SI$ = Solomon Islands dollar.

projects can be implemented and new opportunities identified. Critical to the success of PPPs or joint ventures with SOE participation are robust governance arrangements, full transparency, and arms-length relationships with governments—consistent with SOEs' commercial mandates.

C. IMPROVING STATE-OWNED ENTERPRISE PERFORMANCE

As long as SOEs remain under government control, the risks of political interference and noncommercial decision making remain high. Governments have tried to fix this fundamental flaw by creating legal, governance, and monitoring frameworks to try to mimic the conditions and incentives that private sector firms face. This has been done using different approaches.

There is no consistent legal or institutional framework for SOEs in the countries in this study. In the Pacific, the rules governing SOE behavior are usually established through an overarching SOE Act, based largely on the New Zealand SOE Act.[57] This is true for the SOE Acts of Samoa, Solomon Islands, and Tonga, each of which set common standards and rules on SOE establishment, disestablishment, governance, reporting, management, oversight, and commercial objectives. The SOE legal frameworks in Cabo Verde, Jamaica, Mauritius,[58] and PNG comprise a mix of legislation and codes, and set no clear commercial objective for SOEs.[59] However, many SOEs in these countries are companies and benefit from governance and other provisions contained in their company legislation.[60]

A comprehensive SOE legal framework does not itself guarantee improved SOE performance. Individual examples of successful SOEs can be found in every country participating in this study, even where the formal legal, governance, and monitoring frameworks are weak.[61] Conversely, countries like Samoa with very robust SOE legal, governance, and monitoring frameworks can generate consistently poor SOE results. What appears crucial is the political will to require SOEs to make a positive rate of return and hold them accountable for results. When this will exists, a robust SOE legal framework facilitates

57 State-Owned Enterprise Act 1986.

58 The SOE legal framework in Mauritius includes the Companies Act, Financial Reporting Act 2004, Statutory Bodies (Accounts and Audit) Act 1972, and the Code of Corporate Governance for Mauritius.

59 The SOE laws in Cabo Verde and Jamaica lack many core provisions—focusing mainly on financial, reporting, and audit. The framework in Mauritius contains many of the provisions found in a comprehensive SOE Act.

60 Appendix 4 summarizes SOE legal frameworks in each country in the study.

61 Air Terminal Services (Fiji), Fiji Electricity Authority, Eda Ranu (PNG), Marshall Islands Development Bank, Mauritius Airports, National Pharmaceutical Product Company (Cabo Verde), Port Authority of Jamaica, Samoa Shipping Corporation, Solomon Islands Electricity Authority, and Tonga Power.

Box 14: Features of Robust State-Owned Enterprise Legislation

State-owned enterprise (SOE) legislation should cover:

- SOE establishment;
- SOEs' primary commercial objective;
- Selection, appointment, and removal processes for directors;
- Directors' roles and responsibilities;
- Conflict of interest management;
- Chief executive officer appointment;
- Responsible and shareholding ministers' roles;
- Content and approval process for
  - business/corporate plans,
  - statement of corporate objectives/intent,
  - annual (and semiannual) reports,
  - audit requirements, and
  - performance review/audit;
- Reporting requirements to parliament and public accountability; and
- Definition, approval, costing, contracting, and funding community service obligations.

commercial outcomes (Box 14). When the will does not exist and SOE laws are ignored, continued poor performance is sanctioned.

There is increasing evidence that, in the long run, good corporate governance rests squarely on a foundation of law and regulation.[62] Under a good legal framework, laws that govern business transactions can do much to support commercial activity. Most generally, laws should set out requirements that align incentives with social needs to produce socially useful behavior, including that which governs SOE operations. Business laws also establish enforcement mechanisms that work well within a country's political and economic constraints. Importantly, they provide templates for commercial transactions that reduce transaction costs. Countries and regions in which legal systems function effectively have an advantage in encouraging both local and foreign investment, over those countries where the law is opaque, slow, and costly. Although SOEs have the state as their sole or primary shareholder, the same principles apply. If well-implemented, a sound legal foundation will promote more effective operation.

Many countries are introducing legislation, ownership rules and guidelines, governance practices, and monitoring structures to place SOEs on a firm commercial footing.

- **SOE legislation.** Since 2005, new or significantly enhanced SOE laws have been adopted or developed in Cabo Verde, the People's Republic of China, Finland, Hungary, Kiribati, the Republic of Korea, Namibia, Tuvalu, Norway, PNG, Poland, Portugal, Solomon Islands, Spain, Switzerland, and Tonga.

- **Ownership rules and disclosure.**[63] Since 2005, rules or guidelines have been introduced in Finland, the Republic of Korea, Norway, Poland, Portugal, and Spain defining the state's ownership role, establishing SOE performance criteria, and increasing the transparency of reporting relative to performance targets. The Republic of Korea has introduced an online system to provide real time information on SOEs' financial and nonfinancial performance, and New Zealand has moved to a continuous disclosure regime for its seven largest SOEs. Finland, France, Ireland, New Zealand, Norway, Sweden, and Turkey now produce comprehensive public reports on their SOEs' performance, performance criteria, and the major policies that apply to the SOEs' operation and control.

- **Governance practices and expectations.** Codes of practice that incorporate conflict of interest guidelines, skills-based board selection and appointment requirements for SOE boards, and rules limiting the ability of politicians to direct SOEs have been introduced in over a dozen countries. Many countries have adopted the Organisation for Economic Co-operation and Development guidelines on good corporate governance.

- **SOE monitoring structures.** Centralized monitoring properly separates the ownership function from regulation, and assists the government in implementing its ownership policy. Centralized monitoring also enables the development of specialized SOE ownership monitoring expertise. In Latin America, for example, most countries are moving to a more centralized model.[64]

[62] See G. Walker and T. Reid. 2002. Upgrading Corporate Governance in East Asia—Part 1. *Journal of International Banking Law*. 17(3). pp 59–66.

[63] See Appendix 3 for an expanded list of reforms since 2005.

[64] L.A. Andrés, J. Schwartz, and J.L. Guasch. 2013. Corporate Governance of State-Owned Enterprises. In L. Andres, J. Schwartz, and J.L. Guasch, (eds). *Uncovering the Drivers of Utility Performance: Lessons from Latin America and the Caribbean on the Role of the Private Sector, Regulation, and Governance in the Power, Water, and Telecommunication Sectors*. Washington, DC: World Bank.

Box 15: How Is Competitive Neutrality Applied to State-Owned Enterprises?

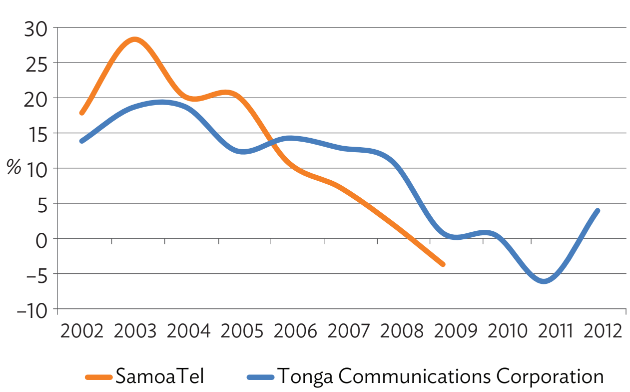
- State-owned enterprises (SOEs) have no preferential access to government contracts, nor the requirement to deliver community service obligations without market-based compensation.
- There are no government guarantee or soft loans for SOEs.
- Government equity is priced as in comparable private firms.
- SOEs are subject to the same labor and tax rules as the private sector.
- SOEs do not benefit from protective barriers.

D. ESTABLISHING COMPETITIVE NEUTRALITY

In some SOEs, profitability is not due to operating efficiency but results from monopolies that are enshrined in law. Both SamoaTel and Tonga Communications Corporation (TCC) are examples of SOEs that accounted for a large part of the profits of their country's SOE portfolios. Once effective competition was introduced, the performance of both SOEs fell precipitously (Figure 29).[65]

This illustrates the principle of competitive neutrality: that the same competition criteria should be applied to SOEs as to private companies. Monopoly rights and privileges granted to SOEs shelter them from market forces, so that their profitability could result solely from their market power. SOEs should not enjoy competitive advantages over their private sector competitors—without objective justification—simply by virtue of their state ownership. Lack of competition weakens SOE incentives to improve efficiency and profitability.

Figure 29: Return on Equity of SamoaTel and Tonga Communications Corporation, FY2002–FY2012[a]



FY = financial year.
[a] Data for SamoaTel is unavailable after 2009, following its 2010 privatization.
Source: State-Owned Enterprise Monitoring Division, Ministry of Finance (Samoa).

[65] For SamoaTel, privatization in 2010 brought in much-needed capital and management expertise, allowing it to more effectively compete. TCC's performance continues to decline as the government debates whether to privatize it.

In small island economies, many SOEs have monopolies in their markets, such as water, electricity, airports, and ports. Some long-term legislative barriers to competition have provided SOEs with significant advantages over private sector operators.

The most effective way of dealing with this problem is to establish a legal framework for competition, which includes SOEs. For example, all SOEs in the European Union (EU) are subject to its Competition Framework (Box 16). The EU adopts a comprehensive legal framework supporting competitive neutrality. SOEs are not to receive subsidies, grants, or other types of financial support that would favor them over competitors that do not benefit from state support. Pacific island countries are still developing these institutional structures.

Box 16: Enforcing Competitive State-Owned Enterprise Neutrality in the European Union

The European Commission enforces its rules and regulations to support competitive state-owned enterprise neutrality, and the delivery of CSOs in particular. Between 2005 and 2011, the commission made 15 state-aid decisions on postal operators, 16 decisions on public service broadcasters, and 12 decisions on CSOs in the financial services sector. These focused on whether public service obligations as part of these contracts were carried out at the *least* cost to the community.

The commission receives many complaints on this issue annually, illustrating the demand for rigorous enforcement.

E. COMMUNITY SERVICE OBLIGATIONS AND STATE-OWNED ENTERPRISE PERFORMANCE

In many countries in this sample, SOEs are required to provide services to communities on noncommercial terms. Such services—known as CSOs—are sometimes only partially compensated, or SOEs are expected to provide them with no compensation. For others there is compensation, but there is no competitive tendering. Both practices have negative effects. If there is incomplete compensation, SOE performance is

Box 17: Features of Effective Community Service Obligation Practices

- Full costing of the community service obligation (CSO), including capital costs;
- Funding to ensure that CSOs do not undermine state-owned enterprise commercial mandates;
- Explicit government directives for each CSO; and
- CSO delivery monitored against the performance measures in the contract.

negatively affected through reduced rates of return and the excuse it provides SOE management for poor performance. As the country diagnostic sections demonstrate, CSO policies in Cabo Verde, Jamaica, the Marshall Islands, Mauritius, and PNG are poorly defined and unequally implemented. They are a major cause of poor SOE performance. In contrast, the CSO process in Solomon Islands is robust and has contributed to the portfolio's relatively strong performance (Box 17).

Where there is compensation for CSOs but no competitive tendering, this violates competitive neutrality. CSO rules should encourage competitive tendering. However, CSO rules often contemplate an SOE providing the good or service, rather than seeking alternative providers. Competitive tendering ensures public money is spent effectively and channeled to the most economically advantageous CSO provider.

F. GOVERNANCE AND MONITORING

The 2008 financial crisis revealed how failures in corporate governance can ruin firms and have an economy-wide impact. Corporate governance practices matter, as does the monitoring of the uses of capital. Good corporate governance should maximize firms' contributions to the overall economy. This principle fits neatly into the objective of maximizing the rate of return on the assets controlled by SOEs.

Governance practices designed to improve reporting, accountability, and independence from political interference have boosted SOE performance in the Pacific. Removing elected officials from SOE boards and introducing skills-based director selection and appointment have been important developments. While they have not eliminated the risk of political interference, they have made such interference more difficult and transparent.[66] Similarly, implementing corporate planning and reporting processes in SOEs has made it easier to hold SOEs accountable for performance. SOE board composition in the survey countries illustrates that all but two countries in the survey have removed all elected officials from

Table 13: State-Owned Enterprise Board Composition, 2013

Indicator	Cabo Verde	Fiji	Jamaica	Marshall Islands	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Number of SOEs	15	26	22	11	20	8	27	8	15
Number of directors	46	87	242	73	164	50	176	53	59
Women directors (%)	19.6	10.3	30.6	21.9	3.7	10.0	18.2	13.2	16.9
Number of elected officials serving as directors	0	0	0	22	0	0	0	0	2
Number of public servants serving as directors	18	18	29	12	82	2	20	3	7
Elected officials/public servants on boards (%)	39.1	20.7	11.9	46.6	50.0	4.0	11.4	5.7	12.5
SOE Portfolio ROA 2012 (%)	(6.8)	2.9	(0.7)	(5.0)	2.0	2.7	(0.1)	10.2	3.5

( ) = negative, ROA = return on assets, SOE = state-owned enterprise.
Sources: SOE monitoring units of each country.

66 In Samoa, all 20 elected officials on the boards of SOEs in 2010 had stepped down by 2012. Similarly, in Solomon Islands, all 11 elected officials on SOE boards in 2010 had stepped down by 2012.

SOE boards (Table 14). As these are relatively recent developments, it is too early to see their impact on SOE portfolio performance.

Women continue to play a minority role in SOE boards and management. Jamaica and the Marshall Islands have the highest percentage of women on SOE boards, but one cannot establish causality between this and the poor SOE performance in these countries. Efforts to expand the pool of women available to serve on SOE boards, as is occurring in Solomon Islands, should be encouraged to enrich the mix of skills and experience available to SOEs.

Robust ownership monitoring practices protect the state's investment in SOEs. Globally, there are three ways to monitor SOE performance. These can be summarized as the decentralized, dual, and centralized models.

(i) **In the decentralized model, the sector or line ministry monitors performance and reports to the minister.** The minister of energy, for example, would be responsible for the electricity SOE and would act as the performance monitor. This model has weaknesses; the minister has a conflict of interest in balancing the roles of sector regulator and owner. Since other ministries will also have SOEs in their mandate, monitoring skills will be spread among the various ministries and there is no coordinated SOE oversight or policy.

(ii) **In the dual monitoring model, the sector ministry and ministry of finance share the monitoring oversight role.** This is to reduce the sector minister's conflicts of interest. The advantage over the decentralized model is that the government is better able to take a "whole of government" view of its SOE portfolio, consolidate financial reporting data, and develop economy-wide SOE policies and practices. The weakness is that the sector minister still retains significant control. Ownership monitoring is still spread among multiple ministries, diluting expertise. The Ministry of Finance also has a conflict, being responsible for fiscal discipline and oversight of the SOE portfolio. This model is found in many Latin American countries, as well as Cabo Verde, Fiji, Jamaica, Mauritius, Samoa, Solomon Islands, and Vanuatu.

(iii) **The centralized monitoring model relies on an SOE ministry or a monitoring unit within the Ministry of Finance or Prime Minister's Office.** Holding companies can also be formed to fulfill this role, as in Hungary, PNG, Peru, and Singapore.[67] In Finland, the central ownership monitor sits within the Prime Minister's Office, but reports to the Minister of Defense. No SOE is involved in defense, so that minister has no conflicts of interest. Some private sector firms may be contracted to undertake the ownership–monitoring role, or provide specialist support for the centralized monitor (Box 18).[68]

Box 18: Characteristics of Effective State-Owned Enterprise Ownership–Monitoring Frameworks

- A centralized independent monitoring agency focused on holding state-owned enterprise (SOE) boards accountable for performance;
- Financial and nonfinancial performance targets;
- Monitoring based on SOE corporate and business plans;
- Rewards for good performance and penalties for poor performance, based on agreed performance targets; and
- Timely public disclosure of SOE performance.

The benefits of centralized monitoring are increasingly recognized and a growing list of countries has adopted this model. The current list is Australia, Austria, Belgium, Denmark, France, the Netherlands, Norway, Poland, Spain, and Sweden.[69] In the Pacific, only New Zealand, PNG, and Tonga have adopted this model, although Fiji and Samoa are establishing it in 2014. A centralized ownership–monitor does not guarantee better SOE performance, but it does encourage more effective monitoring. To improve SOE performance, the owner must act on the monitoring output and hold boards to account.

[67] In PNG, a trust owns the SOEs and the trustee is a government-owned company. The SOE holding company in Singapore, Temasek Holdings, began as an SOE holding company but now operates as a sovereign wealth fund with the majority of its investments outside Singapore.

[68] The Auckland Regional Services Trust, an SOE holding company, contracted private sector experts to support its monitoring function.

[69] Forfás. 2010. *The Role of State Owned Enterprises: Providing Infrastructure and Supporting Economic Recovery.* Dublin.

V. BEST PRACTICES AND THE WAY FORWARD

This study has found that, in many countries, SOEs impose large economic and social costs in terms of forgone growth, efficiency, diverting resources that could be used for social expenditure, and damaging the private sector through the inefficient provision of inputs. However, it also demonstrates that improvement is possible.

Privatization, supported by robust regulatory arrangements, has led to long-term improvements in the productivity of state assets worldwide. Transitioning state assets to private control should remain an underlying goal for the countries participating in this study.

While SOEs remain under government control, however, their performance will be improved by placing them on a fully commercial footing. This requires strong political commitment to require commercial rates of return from SOEs, give them the independence to achieve these returns, and hold them accountable for results.

SOE legal, governance, and monitoring frameworks can support the achievement of commercial results when the political will to implement them exists. The countries participating in this study all have some elements of best practice legislation, governance rules, and/or monitoring structures, each of which is implemented with varying degrees of success. These provide valuable guidance and lessons for governments seeking to improve SOE performance.

- **SOE Legislation.** Pacific islands countries have developed best practice SOE legislation. The SOE Acts in Tonga, Samoa, and Solomon Islands represent a good balance between effective state oversight and the commercial independence of the SOE board. The laws require SOE boards to generate profits comparable to private sector firms, while the state's oversight is effective and transparent. Comprehensive CSO provisions reinforce the SOE's commercial mandate, and provide a legitimate and non-distortionary means for the state to purchase social outcomes from SOEs. PNG has recently adapted a CSO policy based on similar principles. However, implementation of certain provisions of the SOE Acts remain challenging in all countries—particularly the CSO provisions and commercial mandate of SOEs in Samoa.

- **Governance rules.** The governance rules in a number of the benchmarked countries reflect global best practice. This includes the skills-based director selection and appointment process in Solomon Islands, where SOE regulations specify that only the best-qualified candidate can be appointed to fill a vacancy. The Independent Selection Committee in Samoa comprises three private sector members responsible for the director selection process, up to the point of identifying the preferred short-list candidates. Cabinet can then only appoint from the Committee's short-list. Tonga has issued a Cabinet directive combining the best aspects of the Solomon Islands and Samoa director selection processes. The governance codes adopted in Mauritius and Jamaica are comprehensive and contain guidelines on board composition (diversity and gender), and codes of ethics and social responsibility. SOEs in Mauritius must report the implementation of the code in their annual reports. The Marshall Islands' SOE law will, when enacted, codify conflict of interest provisions and a code of ethics for directors and staff.

  In Samoa, Solomon Islands, Fiji, and Tonga, Ministers are restricted by law from sitting on SOE boards, which is essential to reducing the risks of politicization of the SOEs.[70] Jamaica's Corporate Governance code goes further by prohibiting permanent secretaries from serving on SOE boards. As with legislation, implementation of governance rules remains difficult, but the dramatic strengthening of the SOE boards in Samoa, Solomon Islands, and Tonga since 2009 demonstrates what is achievable.

- **Monitoring.** The Ministry of Public Enterprises in Tonga appears to be the most effective ownership monitor amongst the benchmark countries. It is the only centralized SOE monitor, and is independent of the Ministry of Finance and sector ministries. The SOE Minister is solely responsible for the SOE portfolio, although Cabinet must consent to the appointment of SOE directors, the approval of CSOs, the change of status of an SOE, and any privatization. These arrangements have allowed effective monitoring to date, but depend on a constructive working relationship between the minister and Cabinet.

[70] Ministers cannot be appointed to SOE boards in Fiji. In Samoa, Solomon Islands, and Tonga, ministers can only be appointed under very limited circumstances and, in the case of Tonga, for no more than 12 months.

- **Transparency.** Transparency and accountability can change behavior—Solomon Islands and Tonga require SOEs to publish copies or summaries of their planning documents and annual reports in local newspapers. The IPBC in PNG is required to publish both the SOEs' annual reports and its own on its website. In practice, only Tonga is doing this systematically. The requirement to negotiate SCIs with SOE boards provides a good practice mechanism for the state as owner to influence direction, and hold boards to account, without undermining the SOE's commercial mandate. This balance is effectively achieved in Tonga and Solomon Islands where responsible ministers can influence, but cannot direct the content of these plans. Jamaica, Mauritius, and Cabo Verde are adopting a similar practice through the use of performance contracts.

Recognizing that SOEs are not a sustainable service delivery model, Jamaica has developed a privatization policy, PNG has a PPP policy, and Fiji and Mauritius have PPP laws. These policies and laws are designed to facilitate greater private sector participation in the SOEs and their services, and are fully compatible with the governments' commitments to deliver CSOs. Indeed, these policies and laws are designed to encourage greater efficiencies in CSO delivery.

- **Jamaica's privatization policy represents good international practice.** It requires post-privatization audits in the case of partial divestments, to ensure what was expected eventuates, and to provide a useful feedback loop for future privatizations. Jamaica is the only country with a formalized privatization transaction guideline, and its policy requires the government to disclose how it will use any privatization proceeds. The DBJ appears to have effectively implemented the policy since it was put in charge of the program in 2006. While other benchmarked countries have successfully privatized some of their SOEs, the absence of a privatization policy and clear transaction rules has inhibited the development of a transaction pipeline.

- **The benchmarked countries have been implementing PPPs over the decade since 2005, but few have formal polices and/or laws to guide these transactions.** PNG's PPP policy reflects international best practice, but it cannot be implemented without accompanying legislation. This legislation has been awaiting submission to Parliament for several years. In Fiji, the 2006 PPP law has yet to be implemented, and includes restrictions on foreign participation that will limit its effectiveness. In Mauritius, the PPP law has been in place since 2004, but the absence of effective institutional arrangements has constrained its implementation. Even in the absence of formal PPP policies and laws, Pacific countries have successfully structured simple PPP transactions. Performance-based service contracts for subsidized shipping services are in place in Fiji, Tonga, Solomon Islands, and PNG. Sound procurement rules, modern contracting law, and cost effective dispute mechanisms can provide a sufficient legal framework for PPP transactions in smaller economies. For economies looking to prepare a pipeline of PPP transactions, a formal PPP law is essential to creating transparency, predictability, and efficiency in the process, thereby reducing investor risk and transaction costs.

An effective and well-functioning competition framework is important in promoting SOEs' efficient operation. The framework ensures that: (i) SOEs cannot profit from their market power; (ii) they are required to invest in order to maintain their dominant position; (iii) they are required to improve their productivity; and (iv) they cannot receive undue favors from government. These parameters will be a powerful tool in promoting more efficient operation. The introduction of effective competition frameworks is beginning in the Pacific region; Samoa being the first. Other countries are also realizing the benefits of competition law and regulation, so the extent to which these are used will grow over the next few years.

The experience of the nine countries participating in this study demonstrates that the commercial operation of SOEs is possible, but requires sustained political commitment to enforce the requirements of the underlying SOE legislation, resist the temptation to directly interfere in the business of the SOEs, and allow greater private sector participation in delivering goods and services traditionally provided by SOEs. Increased private sector participation and privatization is the best mechanism to lock in the gains from commercialization. These reforms are achievable, and will generate significant economic and social benefits.

Appendix 1

COMMON MYTHS OF STATE-OWNED ENTERPRISE REFORM

Over the years, myths have evolved to argue against state-owned enterprise (SOE) reform. Critically testing these myths is an important step in securing broad-based commitment to reform.

Myth 1: SOEs should not strive to provide a commercial return; they should instead focus on delivering essential services to the people.

Most SOEs are created through a process of corporatizing government departments or agencies to provide more transparency, accountability, and better efficiency incentives for the delivery of goods or services. **To argue that SOEs should not provide a commercial return argues against the efficiency incentives that corporatization provides.** This argument also implies that SOE profitability is incompatible with public service delivery, which is incorrect. Without the objective of a commercial return, it is difficult for SOE management and directors to perform in a fiscally responsible way.

Best practice SOE legislation establishes the commercial objective for all SOEs as the primary objective. Without a clear commercial focus, decisions will be made that destroy value and progressively compromise the ability of the SOE to provide the goods or services that it has been mandated to deliver. These negative consequences can be seen in many of the SOEs reviewed in this study, which have become dependent on regular cash injections from their shareholder governments to maintain operations.

Myth 2: Only SOEs can fulfil community service obligations (CSOs); if SOEs are commercialized or privatized, CSOs will be discontinued.

It is argued that because CSOs are, by definition, non-commercial activities, only the government (including SOEs) can provide them. This is flawed thinking. There is a difference between the government *financing* CSOs and the government *delivering* CSOs. Just because CSOs cannot be financed solely through user fees does not mean that the private sector cannot provide them; it only means the private sector cannot provide them without a subsidy. Because SOEs are required to operate as commercial enterprises, they also require a subsidy to provide CSOs.

It is in government's best interest to contract the delivery of CSOs to the most efficient and cost effective provider, which may or may not be an SOE. The competitive tendering of CSO provision, where feasible, will result in a more cost effective outcome. For example, in Solomon Islands, the tendering of contracts for interisland shipping services resulted in multiple bids and successfully awarded contracts to private providers. In Fiji and Tonga, private companies provide subsidized shipping under contract to the government. This process has allowed the subsidy to be reduced over time as the volume of users increase, making the services more commercially viable, without any decline in quality.

Myth 3: The process of commercialization is not achieving the promised benefits.

The continued poor performance of SOEs is often cited as evidence that corporatization and commercialization are not working. This is misleading, however, because the benefits of SOE corporatization and commercialization have been well demonstrated throughout the world. Three decades of SOE creation and reform demonstrate that governments throughout the world see benefits in commercializing certain state activities and establishing frameworks to optimize their performance. In New Zealand, case experience strongly suggests "there were major gains in efficiency from corporatization that were distributed among customers and owners. The movement in real prices and service levels show that customers were major beneficiaries from the changes. The swing from making no return to the government as owner and making substantial payments in dividends and taxes meant that citizens as owners were a major beneficiary also."[1]

There are many examples of the gains that can be achieved through an effective commercialization process (for example, Fiji International Communications [FINTEL], Mauritius Telecom, National Bank of Vanuatu, Samoa Broadcasting Corporation, and Tonga Power). There are also many instances where establishing an SOE has failed to result in the level of improved performance sought.

[1] G.C. Scott. 1996. Government Reform in New Zealand. *Occasional Paper No. 140*. Washington, DC: International Monetary Fund.

Why are the gains from SOE commercialization not being seen in every case? In many instances, SOE commercialization is still incomplete. Simply transferring a set of activities from a ministry or government department into an SOE corporate structure will not result in improved efficiencies and service delivery, unless a conducive policy and regulatory framework exists and is implemented. This framework would include

(i) an SOE policy setting out the government's expectations on how the SOE portfolio and individual SOEs will be managed to maximize shareholder value, and achieve all of the benefits sought from the corporatization; and

(ii) an SOE act establishing a commercial focus for SOEs, governance principles under which they will be managed, and reporting and accountability structures; and also identifying a minister to be responsible for the "ownership" interest in the SOE, and establishing effective "ownership" monitoring oversight.

While four of the nine countries participating in this study have SOE policies and enabling legislation that contain the core previsions listed, they are not being fully implemented. Consequently, while SOEs have been corporatized, many do not operate with management independence, profit orientation, hard budget constraints, or accountability for results. The commercialization process has been started but not completed, leading to the negative performance outcomes observed. A core finding from this study is that SOE performance is a function of how quickly and completely governments implement robust SOE policy and regulatory frameworks.

Myth 4: SOEs are vital generators of employment.

There is a fear that privatizing or reforming SOEs will result in layoffs and reduced employment. This argument is flawed:

(i) Public employment crowds out private employment. Studies of developing and advanced countries demonstrate that a public job typically comes at the cost of a private sector job. Public sector hiring (a) does not reduce unemployment, (b) increases the fiscal burden, and (c) inhibits long-term growth through reductions in private sector employment.[2] Public hiring, or retaining surplus staff in SOEs, is harmful to long-term fiscal sustainability and has limited benefits. Scarce resources would be better spent on higher value social needs, such as protecting the most vulnerable.

(ii) If the SOE is providing valuable goods or services, those goods or services will be required post-privatization, and employees will continue to be required. Some restructuring may result in rationalizing the workforce, but this will lead to the private successor being more competitive and able to sustainably grow and expand its workforce in the future.

(iii) The SOE portfolios in all of the countries taking part in this study are failing to achieve a reasonable return on their assets: they are not contributing to overall economic growth. Continued government ownership in underperforming SOEs is actually limiting the opportunities for job creation.

(iv) The private sector is the engine for economic growth, and will generate sustainable growth in employment. As this study shows, governments' continued ownership of commercial SOEs can crowd out the private sector and stifle growth, thereby stifling employment generation.

Total employment in the New Zealand economy grew by 22% during 1988–2004, when significant privatization activity occurred.[3] While privatization may reduce employment in individual SOEs, the broader impact of SOE reform supports economic expansion and employment growth.

Myth 5: Privatization results in increased tariffs for public services.

Some argue that increased private participation in providing public services will result in increased prices for those services. While tariff increases may follow privatization or SOE reform, such as in public–private partnership (PPP) arrangements, there is no evidence to suggest that there is a direct cause and effect. Services cost money. When an SOE provides services at a tariff that does not allow it to recover the full costs, the SOE is unable to make the investments required to maintain infrastructure, improve service quality, and expand access. This does not result in cost savings, but rather a deferred cost because money will need to be invested to maintain these services at some future time. Often, the longer it takes to make this investment, the greater the actual cost to be borne by taxpayers.

[2] A. Behar and J. Mok. 2013. Does Public-Sector Employment Fully Crowd Out Private-Sector Employment? *CSAE Working Paper WPS/2013-20*. Centre for the Study of African Economies, Department of Economics: University of Oxford.

[3] P. Barry. 2004. Does Privatisation Work? *Policy Backgrounder No. 5*. New Zealand Business Roundtable. December. Downloaded at http://www.nioclibrary.ir/privatization/e009.pdf

If the private sector is contracted to provide (even expand) services, it will only do so if it can cover its costs of delivery and make a profit. If tariffs are capped at rates that do not allow this full cost recovery, then a CSO subsidy will be required. This would be the same whether the private sector or an SOE operating under a commercial mandate provided these services. Where tariffs have undergone sharp increases following privatization, this has almost always been due to a concurrent change in the government's tariff policy, where a decision has been made to reduce the level of subsidy for consumers.

Extensive analysis of the impact of private participation in public service delivery internationally—particularly in utilities—reveals increased efficiencies and lower costs of delivery, resulting in improved value for money for government funders. These savings can then be passed onto consumers.

Myth 6: Public servants and elected officials play a vital role on SOE boards.

Public servants serve as directors on the boards of SOEs in Cabo Verde, Jamaica, Mauritius, Samoa, and Tonga. In Fiji, public servants are appointed as directors and sit as observers to SOE boards. Public servants and elected officials serve on SOE boards in the Marshall Islands. Two reasons are often given to justify this practice: (a) public servant board members or observers play a useful role in keeping the responsible minister fully informed on what is happening within the particular SOE; and (b) public servants bring vital skills and knowledge to the boards, particularly where they are employed by the ministry responsible for the economic sector in which the SOE operates.

While true that public servants can bring useful knowledge to an SOE board, there are risks with this practice that make it undesirable:

(i) **Conflicts of interest.** Ministers who are both SOE chairs and responsible ministers[4] violate basic principles of good governance. First, SOE ownership responsibilities (as exercised by the responsible or shareholding minister) should be separated from SOE management responsibilities (as undertaken by the board of directors). Second, senior public servants who serve on an SOE board also violate the principle of separation between ownership and management, particularly if they have any public service responsibility for the sector in which the SOE operates. Third, it is impossible for public servants to monitor SOEs effectively if they report to ministers or more senior public servants who serve on those SOE boards.

(ii) **Time constraints.** Public servants are full-time employees, and serving on an SOE board requires a reasonable time commitment—up to 3 days a month for directors and 5 days a month for a chair. Multiple board appointments unreasonably burden the public servant.

(iii) **Liabilities.** The practice of having monitoring agency staff as observers on SOE boards creates special complications: the public servant is caught in the middle. While they are not legally directors, they could be "deemed" as directors and thereby carry all the risks and responsibilities of directors.

The SOE acts in Samoa, Solomon Islands, and Tonga have effective statutory mechanisms that allow and empower the shareholding or responsible minister to exert a reasonable degree of influence over the SOE's strategic direction.

In a well-functioning "owner" monitoring and governance regime, it is unnecessary for a public servant to sit on a board to pass on information to the minister or guide the SOE board. If a public servant has special skills or knowledge that could assist an SOE, it is better that those skills be "contracted" to the SOE rather than making them available through an appointment as a director.

Myth 7: There is insufficient depth in the private sector to populate SOE boards.

A shortage of experienced, qualified directors in the private sector is often cited to justify the continued appointment of elected officials and public servants to SOE boards. While a limited pool of experienced private sector directors is often a reality in smaller countries, the assumption should be tested. In Samoa, 180 new SOE board appointments were made in 2011 to replace public servants and ministers who were required to resign from SOE boards.

The pool of qualified directors can and should be expanded over time, with ongoing director training programs and—where the critical mass exists—institutes of directors, as in Fiji, Jamaica, Papua New Guinea, and Samoa. In addition, expatriate directors can be used to mentor boards and develop directors, often cost effectively.

[4] The "responsible minister" is the minister responsible for SOEs generally, or for a specific SOE.

Myth 8: Only profitable SOEs can be successfully privatized; SOEs must be restructured before sale so that they can generate maximum proceeds.

The privatization of the Samoa Broadcasting Corporation and Sasape Marina demonstrates that unprofitable SOEs can be sold successfully. These SOEs were loss-making when sold, but the new owners have been able to establish viable businesses. Had the SOEs been restructured before sale, there is no guarantee that they would have fetched higher sales prices. The SOE market price, or its assets, is based on the future revenues the new investor believes can be generated from the SOE's assets, not on what the previous owner thought could be generated after restructuring, or had been generated before restructuring. International experience has shown that pre-privatization restructuring rarely returns the sought-after price premium.

Myth 9: Privatization means that governments forgo future dividends from the SOE, and these represent a high opportunity cost.

The sale of an SOE generates cash for the government equivalent to the value of the asset sold—whether the divestment is a full or partial privatization, or an asset sale. Simply, the value of the asset is equivalent to its ability to generate cash over its expected economic life. The sooner the government sells the SOE, the sooner it can realize that cash value and reinvest it back into core social services or repay government debt. The sale of an SOE does not result in the loss of an asset, but the realization of its cash value.

Commercial businesses carry commercial risks. There is no guarantee that a profitable SOE, paying dividends today, will be profitable in the future. The greater likelihood is that profitability will fluctuate over time. Government owners are not good at assessing and managing commercial risks. A prudent government owner would sell its commercial SOEs, recognizing that a dollar in the bank today is worth more than the promise of a dollar in the future.

Myth 10: Governments need to establish and own SOEs to deal with market failure.

Market failure occurs when a market—left to itself—does not allocate resources efficiently. This is usually caused by one of four factors:

(i) abuse of market power, which can occur when a single buyer or seller significantly influences prices or output;

(ii) where the market does not consider the impact of an economic activity on outsiders;

(iii) provision of public goods, such as defense; or

(iv) incomplete or asymmetric information or high uncertainty.

Except perhaps for providing public goods, the government can usually address market failure through regulation and by introducing policies that encourage private sector investment. Creating and maintaining commercial SOEs are inefficient and ineffective means to address market failure.

Myth 11: SOEs belong to the people.

Policy makers often express the view that SOEs "belong to the people" and that selling them would be like selling "the crown jewels." However, if the assets of SOEs are being used inefficiently—as in many countries in our benchmarking sample—there is no benefit to the people from the state ownership. The welfare of the people is not determined by who owns the assets of the SOEs but, rather, who benefits from outputs generated by the capital, plant, and machinery that SOEs own. If assets under the control of SOEs are used less productively under state ownership than under private ownership, "the people" will benefit far more from their sale to private sector operators who can provide better service at lower cost.

Myth 12: Reform principles cannot be applied to SOEs or economies of significantly different size or complexity.

Thirty years of SOE reform proves that the principles driving good, and poor, SOE performance are universal. Sustained political commitment to achieve commercial outcomes—supported through legal, governance, and monitoring frameworks—will result in improved SOE performance. This has proven to be true, regardless of the size of the SOEs or the economies in which they operate. The complexity of the issues may vary, but the core drivers of success remain constant.

Appendix 2

STATE-OWNED ENTERPRISE PERFORMANCE INDICATORS, 2012

Table A2.1. Cabo Verde: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets ($ '000)	Total Revenue ($ '000)	Asset Utilization (%)	Total Liabilities ($ '000)	Average Return on Equity FY2008–FY2012 (%)
ASA	Empresa Nacional de Aeroportos e Segurança Aérea (National Airports and Air Safety Company)	100	4.1	2.0	17,548	5,717	32.6	8,864	1.1
ATLTUNA	Sociedade Caboverdiana e Angolana de Pesca (Cabo Verdean and Angolan Society of Fisheries)	60	(29.1)	(20.1)	123	22	17.8	38	(3.3)
CABNAVE	Estaleiros Navais de Cabo Verde (Cabo Verde Shipyards)	99	(8.4)	(4.5)	331	379	114.4	154	(1.8)
CCV	Correios de Cabo Verde (Post Offices of Cabo Verde)	100	(10.2)	(6.7)	1,436	283	19.7	501	(0.6)
ELECTRA	Empresa de Electricidade e Agua (Electricity and Water Company)	78	0.0	(8.2)	7,830	6,727	85.9	8,543	(4.0)
EMPROFAC	Empresa Nacional de Produtos Farmaceuticos (National Pharmaceutical Product Company)	100	11.9	6.4	1,439	1,384	96.2	664	5.1
ENAPOR	Empresa Nacional de Administração Dos Portos (National Ports Administration Company)	100	(7.0)	(2.3)	7,620	2,106	27.6	5,154	0.5
FIC	Zona Franca Comercial de Cabo Verde (Commercial Zone of Cabo Verde)	100	0.0	5.0	33	40	123.2	42	0.7
IFH	Imobiliária, Fundiária e Habitat (Real Estate, Land and Habitat)	100	(0.1)	(0.1)	4,200	744	17.7	1,998	(1.0)
INCV	Imprensa Nacional de Cabo Verde (National Press of Cabo Verde)	100	(3.8)	(1.6)	601	128	21.3	342	0.4
INFORPRESS	Agência Cabo-Verdiana de Notícias (Cabo Verdean News Agency)	100	0.0	(12.8)	73	46	62.7	152	(2.6)
RTC	Radiotelevisão Caboverdiana (Cabo Verdean Broadcasting)	100	NA	NA	NA	NA	NA	NA	(3.1)
SDTIBM	Sociedade de Desenvolvimento Turístico das Ilhas Boa Vista e Maio (Tourism Development Corporation of the Boa Vista and Maio Islands)	51	22.3	4.6	5,838	476	8.2	4,628	(0.5)
TACV	Transportes Aéreos de Cabo Verde (Cabo Verde Airlines)	100	0.0	(55.1)	5,827	9,076	155.8	13,141	(9.5)
	Portfolio		**(41.4)**	**(6.8)**	**52,897**	**27,577**	**52.1**	**44,221**	**(3.1)**

( ) = negative, $ = escudo, FY = financial year (1 January–31 December), NA = data not available.
Source: Ministry of Finance and Planning (Cabo Verde).

Table A2.2. Fiji: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (F$ '000)	Total Revenue (F$ '000)	Asset Utilization (%)	Total Liabilities (F$ '000)	Average Return on Equity FY2002–FY2012 (%)
AFL	Airports Fiji Limited	100	7.4	5.6	199,326	63,254	31.7	47,563	2.4
AirPac	Air Pacific	51	8.1	2.0	275,897	347,636	126.0	208,772	2.3
ATS	Air Terminal Services	51	4.0	3.3	16,812	14,025	83.4	2,810	8.7
FBCL	Fiji Broadcasting Corporation Limited	100	(61.5)	(11.4)	28,442	6,672	23.5	23,188	(0.2)
FDB	Fiji Development Bank	100	2.5	0.9	332,750	38,846	11.7	216,593	0.7
FEA	Fiji Electricity Authority	100	13.7	7.3	1,031,482	298,577	28.9	479,588	1.3
FHCL	Fiji Hardwood Corporation Limited	90	(1.3)	(1.1)	134,084	13,226	9.9	23,777	(0.9)
FINTEL	Fiji International Telecommunications Limited	51	14.5	13.4	21,399	11,972	55.9	1,609	12.2
FP	Fiji Pine	100	NA	NA	NA	NA	NA	NA	(2.8)
FPCL	Fiji Ports Corporation Limited	100	7.4	5.1	145,772	50,207	34.4	46,077	2.1
FPFL	Food Processors (Fiji) Limited	100	5.1	1.7	7,748	4,028	52.0	5,113	1.2
FPTCL	Fiji Public Trustee Corporation Limited	100	5.7	5.6	8,591	1,280	14.9	84	3.3
FSC	Fiji Sugar Corporation	68	0.0	(19.5)	133,324	138,834	104.1	200,546	(18.8)
FSHIL	Fiji Ships and Heavy Industries Limited	100	–	–	–	–	–	–	(2.8)
HA	Housing Authority	100	0.7	0.2	172,916	11,165	6.5	120,079	0.6
PAFCO	Pacific Fishing Company Limited	100	(15.8)	(8.4)	28,959	24,646	85.1	13,584	0.8
PFL	Post Fiji Limited	100	2.5	1.1	27,228	24,984	91.8	15,503	1.2
PRB	Public Rental Board	100	7.2	3.2	8,708	3,338	38.3	4,847	12.7
RRL	Rewa Rice Limited	100	0.0	(15.4)	1,758	803	45.7	6,819	(7.4)
UTOFML	Unit Trust of Fiji (Management) Limited	100	20.7	17.0	1,223	1,358	111.0	218	6.5
VCCL	Viti Corps Company Limited	100	NA	NA	NA	NA	NA	NA	(10.4)
YPCL	Yaqara Pastoral Company Limited	100	18.9	17.9	11,934	3,247	27.2	640	9.1
	Portfolio		**6.5**	**2.9**	**2,588,353**	**1,058,095**	**40.9**	**1,417,412**	**0.5**

– = no longer operating or no longer government majority-owned in FY2012, ( ) = negative, F$ = Fiji dollar, FY = financial year (1 January–31 December), NA = data not available.
Source: Ministry of Finance (Fiji); Ministry of Public Enterprises, Communications, Civil Aviation and Tourism (Fiji).

Table A2.3. Jamaica: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (J$ '000)	Total Revenue (J$ '000)	Asset Utilization (%)	Total Liabilities (J$ '000)	Average Return on Equity FY2003–FY2012 (%)
AAJ	Airports Authority Jamaica	100	5.1	1.2	21,700	3,980	18.3	16,515	0.9
AirJAM	Air Jamaica	100	–	–	–	–	–	–	(41.0)
BATCO	Bauxite and Alumina Trading Community Limited	100	5.6	5.4	2,284	227	9.9	65	4.4
CAP	Clarendon Alumina Production Limited	100	NE	(19.7)	30,780	12,806	41.6	43,263	(6.7)
CTL	Caymanas Track Limited	100	NE	(54.4)	535	4,512	843.2	919	(5.4)
DBJ	Development Bank of Jamaica	100	6.5	3.1	22,635	2,754	12.2	11,990	1.5
FCJ	Factories Corporation of Jamaica	100	2.5	1.9	7,139	428	6.0	1,604	2.7
HAJ	Housing Agency of Jamaica Limited	100	5.0	1.0	11,444	1,966	17.2	9,050	(2.6)
JBM	Jamaica Bauxite Mining Limited	100	NE	(11.6)	5,630	2,451	43.5	6,355	(3.3)
JMB	Jamaica Mortgage Bank	100	9.4	5.1	3,319	206	6.2	1,529	0.7
JUTC	Jamaica Urban Transit Corp	100	(90.3)	(17.0)	11,810	3,792	32.1	9,580	(319.5)
NEIBJ	National Export-Import Bank of Jamaica Limited	100	5.4	1.4	7,895	664	8.4	5,869	1.5
NROCC	National Road Operating and Constructing Company Limited	100	NE	14.1	18,947	7,941	41.9	47,185	(8.4)
NWC	National Water Commission	100	NE	(4.6)	44,637	20,330	45.5	46,063	(4.6)
PAJ	Ports Authority of Jamaica	100	5.4	1.4	50,294	13,945	27.7	37,584	4.6
PCJ	Petroleum Corporation of Jamaica	100	9.9	8.7	9,794	1,839	18.8	1,169	4.5
PEL	Petrojam-Ethanol Limited	100	1.6	0.7	1,798	3,410	189.6	1,065	3.4
PetCom	Petroleum Company of Jamaica Limited	100	9.2	3.4	1,489	10,708	719.1	936	2.9
PetroJAM	Petroleum Jamaica	100	17.1	3.1	58,313	172,977	296.6	47,856	5.6
PSC	Ports Security Corps Limited	100	NE	(84.0)	76	517	681.4	222	(16.3)
SCJ	Sugar Company of Jamaica	100	–	–	–	–	–	–	(49.6)
UDC	Urban Development Corporation	100	4.1	3.6	34,010	4,559	13.4	4,082	1.5
WCC	Wallenford Coffee Company or Coffee Industry Board	100	28.0	9.7	418	475	113.7	273	(11.1)
WWL	Wigton Windfarm Limited	100	18.2	2.0	6,236	1,075	17.2	5,547	(0.8)
	Portfolio		**(4.0)**	**(0.6)**	**351,185**	**271,562**	**77.3**	**298,721**	**(3.6)**

– = no longer operating or no longer government majority-owned in FY2012, ( ) = negative, FY = financial year (1 April–31 March), J$ = Jamaican dollar, NE = negative equity.
Source: Public Enterprise Division, Ministry of Finance and Planning (Jamaica).

Table A2.4. The Marshall Islands: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets ($ '000)	Total Revenue ($ '000)	Asset Utilization (%)	Total Liabilities ($ '000)	Average Return on Equity FY2002–FY2012 (%)
AMI	Air Marshall Islands	100	NE	(17.6)	5,842	2,651	45.4	7,149	(22.5)
Kajur	Kwajalein Atoll Joint Utility Resources	100	(16.0)	(11.7)	4,114	7,202	175.0	1,098	(34.9)
MAWC	Majuro Atoll Waste Corporation	100	(22.5)	(19.8)	741	804	108.6	90	(3.6)
MEC	Marshalls Energy Company	100	NE	1.7	17,301	50,798	293.6	28,996	(7.6)
MIDB	Marshall Islands Development Bank	100	11.0	7.6	22,173	3,814	17.2	6,743	3.0
MIPA	Marshall Islands Ports Authority	100	(9.8)	(9.1)	54,831	3,022	5.5	3,916	(1.8)
MISC	Marshall Islands Shipping Corporation	100	NE	76.6	301	2,238	743.9	391	(11.6)
MRI	Majuro Resort	100	NE	(39.8)	1,875	2,363	126.0	2,798	(35.3)
MWSC	Majuro Water and Sewer Company	100	(108.6)	(29.7)	1,085	1,246	114.9	788	7.8
NTA	National Telecommunication Authority	100	(14.5)	(2.3)	36,004	8,602	23.9	30,309	0.4
Tobolar	Tobolar Copra Processing Plant	100	(31.9)	(29.9)	3,549	4,493	126.6	226	(8.1)
	Portfolio		**(11.3)**	**(5.0)**	**147,816**	**87,233**	**59.0**	**82,504**	**(5.6)**

( ) = negative, FY = financial year (1 October–30 September), NE = negative equity.
Source: Annual State-Owned Enterprise Audit Reports (Republic of the Marshall Islands).

Table A2.5. Mauritius: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (Rs '000)	Total Revenue (Rs '000)	Asset Utilization (%)	Total Liabilities (Rs '000)	Average Return on Equity FY2002–FY2012 (%)
AIR	Air Mauritius Limited	59	(34.9)	(7.9)	9,058	11,174	123.4	7,008	(1.6)
AMB	Agricultural Marketing Board	100	30.6	16.0	446	592	132.8	212	5.0
AML	Airports of Mauritius Limited	100	12.5	4.9	17,468	2,015	11.5	10,553	10.1
BPM	Business Parks Mauritius	100	1.7	1.3	4,178	155	3.7	938	3.8
CEB	Central Electricity Board	100	3.3	1.6	26,572	13,529	50.9	13,782	0.8
CWA	Central Water Authority	100	6.0	3.1	8,338	1,701	20.4	4,092	(0.2)
DBM	Development Bank of Mauritius	100	(3.6)	(0.6)	7,402	496	6.7	6,083	0.8
EM	Enterprise Mauritius	100	(0.4)	(0.3)	94	180	190.6	29	(1.1)
MFDC	Mauritius Film Development Corporation	100	(15.3)	(12.5)	9	10	106.0	2	(3.2)
MHC	Mauritius Housing Corporation	100	12.9	4.7	6,464	691	10.7	4,097	2.8
MPA	Mauritius Ports Authority	100	7.3	7.0	8,702	1,407	16.2	373	7.3
MSC	Mauritius Shipping Corporation	100	(55.4)	(21.9)	393	473	120.6	238	(2.8)
NHDC	National Housing Development Corporation	100	3.8	1.4	1,418	283	19.9	904	1.1
NTC	National Transport Corporation	100	NE	3.8	835	1,216	145.6	1,204	(0.9)
RBSEB	Rose Belle Sugar Estate Board	100	(1,214.8)	(8.1)	376	180	47.9	374	(0.1)
RDA	Road Development Authority	100	0.7	0.5	2,054	195	9.5	668	0.4
SIL	State Informatics Limited	100	9.1	3.3	256	271	105.7	163	1.0
SLDC	State Land Development Company	100	9.3	8.6	2,300	540	23.5	161	0.5
STC	State Trading Corporation	100	78.0	14.6	5,095	37,564	737.4	4,141	0.2
WWMA	Waste Water Management Authority	100	(77.6)	(10.2)	340	375	110.1	296	5.3
	Portfolio		**5.8**	**2.6**	**101,799**	**73,047**	**71.8**	**55,316**	**1.9**

( ) = negative, FY = financial year (1 July–30 June), NE = negative equity, Rs = Mauritian rupee.
Source: Office of Public Sector Governance (Mauritius).

Table A2.6. Papua New Guinea: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (K '000)	Total Revenue (K '000)	Asset Utilization (%)	Total Liabilities (K '000)	Average Return on Equity FY2002–FY2012 (%)
ANL	Air Niugini Limited	100	18.2	8.1	886,970	1,131,624	127.6	494,379	4.7
ERL	Eda Ranu Limited	100	10.6	8.5	125,875	104,209	82.8	24,848	4.4
NDB	National Development Bank	100	2.5	2.3	369,863	30,780	8.3	24,921	(12.2)
PNGWB	PNG Water Board	100	7.4	2.5	303,565	60,424	19.9	201,683	1.0
PPCL	PNG Ports Corporation	100	7.5	5.3	1,290,842	276,556	21.4	382,590	4.5
PPL	PNG Power Limited	100	7.5	3.4	1,457,214	734,016	50.4	791,717	3.3
PPNG	Post PNG Limited	100	0.2	0.1	185,692	56,224	30.3	82,509	(6.0)
TPNG	Telikom PNG Limited	100	(8.0)	(4.7)	1,257,350	356,078	28.3	514,694	6.0
	Portfolio		**4.7**	**2.7**	**5,877,372**	**2,749,911**	**46.8**	**2,517,342**	**3.3**

( ) = negative, FY = financial year (1 January–31 December), K = kina, PNG = Papua New Guinea.

Source: Annual accounts of the State-Owned Enterprises, Independent Public Business Corporation (Papua New Guinea).

Table A2.7. Samoa: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (ST '000)	Total Revenue (ST '000)	Asset Utilization (%)	Total Liabilities (ST '000)	Average Return on Equity FY2002–FY2012 (%)
ASC	Agricultural Stores Corporation	100	(4.0)	(2.7)	9,866	3,671	37.2	3,316	1.7
DBS	Development Bank of Samoa	100	(1.8)	(0.7)	134,794	11,472	8.5	80,087	(0.4)
EPC	Electric Power Corporation	100	1.6	1.1	257,310	100,311	39.0	86,273	0.6
PAL	Polynesian Airlines Limited	100	5.0	3.0	30,066	13,162	43.8	12,419	(9.2)
PTO	Public Trust Office	100	7.5	3.1	5,162	900	17.4	3,028	(17.7)
SAA	Samoa Airport Authority	100	(1.5)	(1.4)	58,774	9,502	16.2	4,022	(1.5)
SAMPOS	Samoa Post	100	1.2	0.2	26,676	622	2.3	21,659	3.5
SamTel	Samoa Tel	100	–	–	–	–	–	–	4.3
SBC	Samoa Broadcasting Corporation	100	–	–	–	–	–	–	4.6
SHC	Samoa Housing Corporation	100	3.4	2.0	26,341	3,461	13.1	10,646	2.0
SLC	Samoa Land Corporation	100	0.0	0.0	127,080	5,170	4.1	32,910	0.2
SPA	Samoa Ports Authority	100	(2.4)	(1.9)	122,752	12,012	9.8	24,021	0.1
SSC	Samoa Shipping Corporation Limited	100	9.0	2.1	78,786	23,776	30.2	60,068	5.3
SSS	Samoa Shipping Services Limited	100	NE	(0.2)	9,649	7,297	75.6	12,716	(7.6)
STEC	Samoa Trust Estates Corporation	100	(3.5)	(3.1)	50,743	459	0.9	5,624	0.7
SWA	Samoa Water Authority	100	(0.3)	(0.3)	95,353	22,202	23.3	16,221	(2.6)
UTOS	Unit Trust of Samoa	100	(112.9)	(91.3)	566	63	11.1	108	(30.8)
	Portfolio		**(0.1)**	**(0.1)**	**1,033,916**	**214,081**	**20.7**	**373,119**	**(0.1)**

– = no longer operating or no longer government majority-owned in FY2012, ( ) = negative, FY = financial year (1 June–31 May), NE = negative equity, ST = tala.

Sources: State-Owned Enterprise Monitoring Unit, Ministry of Finance (Samoa); individual state-owned enterprises' published annual reports.

Table A2.8. Solomon Islands: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (SI$ '000)	Total Revenue (SI$ '000)	Asset Utilization (%)	Total Liabilities (SI$ '000)	Average Return on Equity FY2002–FY2012 (%)
DBSI	Development Bank of Solomon Islands	100	–	–	–	–	–	–	(2.2)
SAL	Solomon Airlines Limited	100	(6.2)	(2.3)	190,336	288,620	151.6	119,756	(4.1)
SFPL	Soltai Fishing and Processing Limited	51	–	–	–	–	–	–	(2.4)
SIBC	Solomon Islands Broadcasting Authority	100	13.9	4.2	10,514	7,173	68.2	7,301	(23.7)
SIEA	Solomon Islands Electricity Authority	100	12.8	12.2	516,045	413,957	80.2	26,155	1.5
SIHF	Solomon Islands Home Finance Limited	100	–	–	–	–	–	–	(1.1)
SIPA	Solomon Islands Port Authority	100	38.4	31.9	122,144	99,935	81.8	20,471	4.8
SIPC	Solomon Islands Postal Corporation	100	NE	(12.4)	31,040	9,654	31.1	81,062	(29.6)
SIPr	Solomon Islands Printers Limited	100	–	–	–	–	–	–	(12.9)
SIWA	Solomon Islands Water Authority	100	(7.5)	(2.6)	50,767	50,327	99.1	33,115	(12.7)
SML	Sasape Marina Limited	100	–	–	–	–	–	–	(0.2)
	Portfolio		**14.6**	**10.1**	**920,846**	**869,667**	**94.4**	**287,861**	**(1.3)**

– = no longer operating or no longer government majority-owned in FY2012, ( ) = negative, FY = financial year (1 January–31 December), NE = negative equity, SI$ = Solomon Islands dollar.

Source: Economic Reform Unit, Ministry of Finance and Treasury (Solomon Islands).

Table A2.9. Tonga: State-Owned Enterprise Performance Indicators, FY2012

State-Owned Enterprise		Ownership (%)	Return on Equity (%)	Return on Assets (%)	Total Assets (T$ '000)	Total Revenue (T$ '000)	Asset Utilization (%)	Total Liabilities (T$ '000)	Average Return on Equity FY2002–FY2012 (%)
FISA	Friendly Island Shipping Services	100	76.2	46.3	1,343	4,243	315.9	526	4.2
LDF	Leiola Duty Free	75	–	–	–	–	–	–	7.0
PAT	Ports Authority Tonga	100	7.4	5.5	22,414	7,400	33.0	5,738	2.9
SCPL	Shipping Corporation of Polynesia Limited	100	–	–	–	–	–	–	(14.6)
TAL	Tonga Airports Limited	100	(2.8)	(2.5)	36,803	7,337	19.9	3,915	(0.9)
TAMA	Tonga Assets Managers and Associates Limited	100	(2.2)	(1.8)	9,399	381	4.1	1,731	(0.2)
TBC	Tonga Broadcasting Commission	100	(5.1)	(3.2)	3,845	2,389	62.1	1,421	(2.2)
TCC	Tonga Communications Corporation	100	3.8	3.4	49,449	23,385	47.3	6,032	5.9
TDB	Tonga Development Bank	100	7.0	2.2	61,537	7,209	11.7	42,633	3.1
TFPL	Tonga Forest Products Limited	100	(16.5)	(5.9)	6,459	564	8.7	4,147	(2.1)
TIL	Tonga Investments Limited	100	(12.9)	(4.7)	2,192	667	30.4	1,388	(2.0)
TML	Tongatapu Markets Limited	100	–	–	–	–	–	–	1.8
TMPL	Tonga Machinery Pool Limited	100	–	–	–	–	–	–	(2.6)
Tpost	Tonga Post Limited	100	(1.3)	(1.3)	2,217	565	25.5	87	(0.9)
Tpower	Tonga Power Limited	100	13.4	9.9	65,238	48,329	74.1	17,394	1.9
TPrint	Tonga Print Limited	100	–	–	–	–	–	–	5.3
TWB	Tonga Water Board	100	5.2	5.3	20,010	7,233	36.1	(496)	1.1
WAL	Waste Authority Limited	100	(38.7)	(26.8)	2,893	955	33.0	890	(4.9)
	Portfolio		**4.3**	**3.2**	**283,799**	**110,657**	**39.0**	**85,406**	**3.2**

– = no longer operating or no longer government majority-owned in FY2012, ( ) = negative, FY = financial year (1 July–30 June), T$ = pa'anga.

Source: Ministry of Public Enterprises (Tonga).

Appendix 3

SUMMARY OF STATE-OWNED ENTERPRISE REFORM INDICATORS[a]

SOE Reform Indicators[b]	Cabo Verde	Fiji	Jamaica	Marshall Islands	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Legislation									
Comprehensive SOE legal framework[c]									
Commercial mandate[d]	1	3	1	1	3	4	1	4	4
CSO provisions and guidelines									
SOE legal framework implemented[e]	1	3	1	1	3	3	1	4	5
Monitoring									
Responsible minister									
Effective ownership monitor[f]	1	3	1	1	3	3	2	2	4
SOEs operate within tight budget constraints[g]	1	4	1	1	5	2	1	3	5
Requirement for SCI and/or business plan									
Profit target such as ROE implemented									
Governance									
Skills-based director selection and appointment process operating									
Elected officials cannot serve on SOE boards									
Civil servants cannot serve on SOE boards									
Civil servants appointed to SOE boards on restricted basis									
Good governance principles enforced									
Political commitment to reform[h]	2	2	2	1	3	3	1	4	4

ROE = return on equity, SCO = statement of corporate objectives, SOE = state-owned enterprise.

[a] At mid-2014, there is no overarching governance framework or SOE legislation in the Marshall Islands. SOEs are either established under relevant company legislation, or their own Acts, or both.

[b] When cell color is blue, Indicator statement is true.

[c] Combination of legislation (including Companies Act for SOE registered as companies), regulations, and codes of conduct that together are at least as comprehensive as the New Zealand SOE Act.

[d] Scale of 1 to 5: 1 = not evident, 3 = some evidence of commercial mandate, 5 = mandate stipulated in SOE legal framework for all SOEs, Companies Act, and regulatory contracts.

[e] Scale of 1 to 5: 1 = weak implementation, 3 = partial implementation, 5 = substantial implementation.

[f] Scale of 1 to 5: 1 = not evident, 3 = some evidence of ownership monitor, 5 = effective monitor.

[g] Average government transfers FY2003–FY2012 as % of SOE portfolio total assets. Low or positive % = tight budget constraints. Scale 1 = poor budget constraints, 3 = medium-level budget constraints, 5 = high budget constraints.

[h] Determined by interview, questionnaires completed by participating country counterparts, and observation. Scale of 1 to 5: 1 = weak, 5 = strong level of commitment.

Appendix 4

OVERVIEW OF STATE-OWNED ENTERPRISE LEGAL, GOVERNANCE, AND MONITORING REFORMS, 2005–2012

Issue	Country/Region	Nature of Reform[a]
Ownership policy and monitoring	Africa	SOE Network for Southern Africa formed in 2007 to support regional and national reform
	Bhutan	Established Druk Holding & Enterprises as SOE holding company—2007
	Chile	Measures adopted to protect SOEs from receiving instructions from the government and eliminate preferential treatment for SOEs
	China, People's Republic of	SOE Act 2013
	Colombia	Adopted more centralized and strengthened SOE ownership monitoring in 2010
	Finland	State-ownership Act (May 2007) outlining key principles and operating practices of the State's ownership function
	Kuwait	Privatization Commission established in 2012
	Namibia	SOE Act 2006
	Norway	Official government ownership policy for SOEs published in 2007
	Pakistan	Broad-based SOE reform and privatization program launched in 2011[b]
	Paraguay	Developed performance management contracts (SCIs) for SOEs in 2009/10, with quarterly performance reports, and published monitoring agency's strategic plan on website
	Poland	Draft legislation identifies companies of key importance
	Portugal	Council of Minister's best practice for public companies to increase transparency and encourage improved governance practices—2007
	Spain	Ownership policy for SOEs establishes guidelines for commercial and noncommercial objectives, and outline of the role of shareholding minister and good practices for SOEs including increased transparency—General Rules on the Assets of the Central Government (2009)
	South Africa	South Africa SOE ownership policy developed by President's SOE Review Committee
	Switzerland	Guidelines for SOE governance—Corporate Governance Report 2006
	Uruguay	All SOEs must produce accounts in accordance with 2003 version of IFRS
Categorization of public institutions	Estonia	Legislation forbids SOE boards from taking instructions from government, and business plans are approved through the annual general meeting
	Korea, Republic of	Public Management Act (2007) defines public institutions as commercial, noncommercial, quasi-government, and other. To be an SOE, the entity must be more than 50% owned by state and generate at least 50% of its own revenue and if 85% it would be classified as commercial SOE
	Poland	Bill before Parliament will bring management of SOEs under one Act, SOE activity will be drawn closer to private sector firms, and noncommercialized SOEs will be eliminated
Governance	Australia	Commonwealth Government Business Enterprises—Governance and Oversight Guidelines issued in October 2011
	Colombia	2005 Securities Market law established mandatory governance practices for issuing entities, including partially listed SOEs
	Czech Republic, Finland, Norway, and Sweden	Guidelines for the remuneration and employment conditions of SOE managers implemented

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Issue	Country/Region	Nature of Reform[a]
	General	OECD reports that most of the recent changes concerning board composition and qualification have the effect of limiting the scope for politicization and the use of SOE boards for patronage
	Germany, Italy, Spain, and Switzerland	Introduced rules to enhance the integrity of SOE directors, including provisions regarding conflicts of interest and professional qualifications
	Korea, Republic of	Chair of a commercial SOE must always be an outside director
	Peru	FONAFE,[c] the SOE holding company, approved a Good Governance Code, Code of Ethics, and Code of Internal Control (2006) and, in 2010, established the requirement that at least one SOE director be selected by a private search firm
	Poland	Rules being defined to guide the selection and composition of SOE boards with the creation of a state nomination committee
	Portugal	Strategic guidelines issued for use of management objectives
Transparency and disclosure	Chile	Transparency Act (April 2009) requires all SOEs to provide the same information and comply with same accounting standards as private firms
	Finland, France, Ireland, New Zealand, Norway, and Turkey	Reports published on the performance of all SOEs, including aggregate portfolio information and specific SOE performance; and reports also disclose key ownership and governance policies that apply to the SOEs
	Germany	Establishment in 2009 of a parliamentary committee to oversee the management of SOEs
	Italy	Must be public, transparent, and impartial procedures for SOEs' hiring of staff and purchasing external advice
	Korea, Republic of	Online system introduced in 2005 to provide real time information on the financial and nonfinancial performance of all SOEs
	Middle East and North Africa	Progressive implementation of competition authorities to ensure SOEs compete on level playing field with private sector; increased focus on transparency and accountability—Abu Dhabi Accountability Authority established in 2008
	New Zealand	Continuous disclosure regime implemented in 2010 for the seven largest SOEs
	Poland	Draft legislation to increase transparency on the operation of SOEs
	Sweden	Guidelines for external reporting—SOEs should be as transparent as listed companies, and guidelines based on "comply or explain" 2007
	Switzerland	Comprehensive report on the performance of all SOEs to commence in 2011
	Turkey	Council of Minister's Decree in 2006 directed all SOEs to publish annual accounts and include information on their websites

IFRS = International Financial Reporting Standards, OECD = Organisation for Economic Co-operation and Development, SCI = statement of corporate intent, SOE = state-owned enterprise.

[a] Source: OECD. 2011. *Corporate Governance of State-Owned Enterprises: Change and Reform in OECD Countries since 2005*. Paris: OECD Publishing.
[b] J. Speakman. 2012. SOE Reform: Time for Serious Corporate Governance. *World Bank Policy Paper Series on Pakistan No. PK 4/12*. Washington, DC: World Bank Group.
[c] National Fund for Financing State Business Activity.

Appendix 5

CONTENTS OF STATE-OWNED ENTERPRISE LEGISLATION IN SURVEY COUNTRIES[a]

Topic Covered	Cabo Verde	Fiji	Jamaica	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Relevant legislation	Law No. 47/ VII/2009	Public Enterprise Act 1996	Public Bodies Management and Accountability Act 2003	Statutory Bodies (Accounts and Audit) Act 1972; Financial Reporting Act 2004; National Code of Corporate Governance 2004	Independent Public Business Corporation Act 2002 as amended 2012	Public Bodies Act 2001 and Regulations	SOE Act 2007 and Regulations	Public Enterprise Act 2002 and 2010 Amendment
Establishment of SOEs	Article 37	Section 6–30 and Schedules		Establishing Act or Companies Act		Sections 5, 6		Sections 7 and 8
Primary objective of SOEs		Section 43 and KP1		Section 2 Code of Corporate Governance—Corporate Objective Statement		Sections 8 and 14	Section 5	Section 4
Sale of shares or privatization of SOE					Section 9	Section 7		
Governance								
Appointment process for directors		Sections 31 and 56		Section 2 Code of Corporate Governance	Section 9A	Section 15 and Regulations	Section 6 (Subsections 1, 2, and 3) and Regulations	Sections 12 and 14
– Number of directors				Entity Specific Legislation/ Companies Act	Entity specific legislation	Entity specific legislation		Section 12
– Remuneration of directors				Section 2.8 Code of Corporate Governance	Sections 20 and 46I			Section 12 (2)
– Attributes for selection				Section 2.2 Code of Corporate Governance	Section 9A(6)	Regulations (Schedule 3)	Section 6 and Regulations	Section 14 (1)

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Topic Covered	Cabo Verde	Fiji	Jamaica	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Appointment process for chairs				Section 2.5 Code of Corporate Governance				
Composition of the board	Article 18			Section 2.2 Code of Corporate Governance			Section 6 and Regulations	Section 12 (1)
Role of ex-officio members defined								
– Membership allowed					Section 9A (2) and (6)			
– Membership prohibited								
– Membership allowed conditionally				Code of Corporate Governance			Regulation 8	Section 32
– Membership as observers								
Role of ministers as board members defined								
– Membership allowed								
– Membership prohibited								Section 14 (2)
– Membership allowed conditionally						Regulations (Schedule 3.1)	Regulations 8 and 12 (2)	
Removal process for directors	Article 29				Section 9A (7)	Section 25 and Regulations	Regulation 14	Section 14 (6)
Roles and responsibilities of directors		Sections 57, 105, and KP1	Sections 6, 16, 17, 19, and 19A	Code of Corporate Governance, Companies Act and Establishing Legislation	Section 46C (2)	Sections 16–19	Section 6 and Regulations 17–32	Sections 13, 15, 16, and 17
Managing conflicts of interest				Section 2.4 Code of Corporate Governance		Sections 20, 21, and Regulations	Regulations 25	Section 13 (2)
Appointment of CEO		Section 34						Section 26

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Topic Covered	Cabo Verde	Fiji	Jamaica	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Role of CEO				Section 2.6 Code of Corporate Governance				Section 26
Establishment of Audit Committee			Section 8, 9	Section 3 Code of Corporate Governance				
Establishment of responsible minister	Articles 14, 16, 28, 42, and 44			Section 2 Statutory Bodies (Accounts and Audit) Act 1972 and Section 2 Financial Reporting Act 2004			Section 2	
Roles and responsibilities of responsible ministers	Articles 14, 16, 28, 42, and 44	Sections 49, 58, 78, 109, and Schedule 2		Section 3 Statutory Bodies (Accounts and Audit) Act 1972		As a shareholding minister	Section 7, 11, and 12	Sections 8, 9, 10, 11, and 23
Roles and responsibilities of shareholding ministers	Article 13					Section 31		
Roles of shareholders who are not ministers	Article 13	Sections 61–67			Sections 9, 46B, 46G, 46H, 46I, and 46J			
Monitoring								
Establishment of monitoring unit					Sections 6–9			
Monitoring unit requirements/powers	Articles 14, 15, 40, and 44		Sections 5B and 7A	Office of Public Sector Governance, National Committee on Corporate Governance, Sections 19, 76, and 78 Financial Reporting Act 2004	Section 9	Sections 26 and 28		
Requirements defining content and approval								

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Topic Covered	Cabo Verde	Fiji	Jamaica	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
– Business/corporate plans	Article 16	Sections 89–92	Section 7	Sections 4A and 6A Statutory Bodies (Accounts and Audit) Act 1972, Code of Corporate Governance	Section 46E	Section 22 and Regulations		Section 18
– Statement of Corporate Objectives/Intent	Articles 14 and 51	Sections 93–99				Regulations (Schedule 5.5)	Section 13	
– Annual Report	Article 17	Sections 101–104	Section 22	Sections 6A, 8, and 9 Statutory Bodies (Accounts and Audit) Act 1972	Section 45 and Companies Act	Section 23 Regulations (Schedule 6)	Section 14	Section 19, 20
– Audit requirements	Articles 15, 27, 31, 45	Section 100		Part VI Financial Reporting Act 2004; Section 8 Statutory Bodies (Accounts and Audit) Act 1972		Section 27	Section 20	Section 24
– Performance audit/review	Article 11		Sections 12, 13A, 13B, and 23	Section 5 Code of Corporate Governance		Section 24		
Reporting requirements to parliament		Section 106	Sections 5 and 5A	Section 8 and Code of Corporate Governance; Section 9 (2) Statutory Bodies (Accounts and Audit) Act 1972			Section 17	Section 22
Other								
CSO defined		Sections 69, 70, 71, and KP1				Section 9	Section 2	Section 4
Explicit CSO policy						Sections 9–13 and Regulations	Regulations 33–37	Section 4A
Ability for monitoring agency to recommend policies and procedures binding on SOEs				Code of Corporate Governance		Section 26		

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Topic Covered	Cabo Verde	Fiji	Jamaica	Mauritius	Papua New Guinea	Samoa	Solomon Islands	Tonga
Penalties for noncompliance				Section 79 Financial Reporting Act 2004		Sections 13, 19, and 25	Sections 6 (8) and 8 (4)	
Sale or dispose of main undertaking or subsidiaries		Sections 54, 55						
Clarifies priority where SOE conflicts with entity specific legislation						Composition Act 2012	Sections 25 and 26	Section 6 (2)
Mandatory publication of summary of SCI and Annual Report				Code of Corporate Governance			Section 18	Section 22 (2)

CEO = chief executive officer, CSO = community service obligation, SOE = state-owned enterprise.

[a] At end June 2014 there is no overarching governance framework or SOE legislation in the Marshall Islands. SOEs are either established under relevant company legislation, or their own Acts, or both.

Sources: Cabo Verde: Law No. 47/VII/2009; Fiji: Public Enterprise Act 1996; Jamaica: Public Bodies Management and Accountability Act 2003; Mauritius: Statutory Bodies (Accounts and Audit) Act 1972, Financial Reporting Act 2004, and National Code of Corporate Governance 2004; Papua New Guinea: Independent Public Business Corporation Act 2002 as amended 2012; Samoa: Public Bodies Act 2001 and Regulations; Solomon Islands: SOE Act 2007 and Regulations; and Tonga: Public Enterprise Act 2002 and 2010 Amendment.

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