

Lütkenhorst, Wilfried; Reinhardt, Jürgen

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Wilfried Lütkenhorst and Jürgen Reinhardt\*

# The Increasing Role of the Private Sector in Asian Industrial Development

*In recent years, there has been a powerful trend on the global scene and above all in the Asian region for the private sector in general and private industry in particular to assume a growing, and indeed leading, role in economic and industrial development. This article reviews some recent trends of private investment and privatization policies pursued in selected Asian countries and discusses the implications of private sector-led industrial development for the role of governments and international organizations.*

Many governments – disenchanted with the limited growth dynamics generated by public sector-led industrial development – have turned to stimulating private initiative through far-reaching deregulation and privatization programmes. In industrial restructuring efforts, increased reliance has been placed on market forces within an environment of stronger competition in final product markets, input markets and financial markets. As part of this overall process, import protection has generally declined and many restrictions on foreign direct investment have been lifted.

These trends are reflected in above-average growth rates for private investment in most countries. A recent quantitative survey undertaken by the International Finance Corporation points out that the rebound of *private* investment in the second half of the 1980s was stronger than the recovery of gross domestic investment, implying a shift within total investment in favour of private sector capital formation.<sup>1</sup> From Table 1 it emerges that for a sample of 40 developing countries the share of private in total investment between 1985-1989 rose from 53.2 to 58.4 per cent. This clear upward trend is particularly pronounced in the Asian and Pacific region although with a significant difference between Southeast and East Asia on the one hand and South Asia on the other. Whereas the private investment share more or less stagnated in the latter sub-region, it reached almost three quarters of total investment in Southeast and East Asia – the highest share recorded in any developing region.

The figures presented in Table 1 relate to overall investment shares across all sectors of the economy. To

the extent that industry-specific data on the distribution of private investment are available, these reveal a heavy concentration in the rehabilitation, modernization and expansion of industrial production capacities (manufacturing, mining and construction) and related services. In turn, public investment continues to play a lead role in creating and/or upgrading the required physical infrastructure – increasingly within programmes aimed at redressing disparities which have resulted from the widespread past neglect of regionally balanced development.

As a further result of conducive, increasingly liberal policies combined with excellent business opportunities, there has been a growing flow of foreign direct investment into the Asian and Pacific region.<sup>2</sup> During the 1980s when other developing regions found it increasingly difficult to attract foreign investment, the Asian and Pacific region raised its share to 55 per cent of total flows to developing countries (cf. Table 2).

## Privatization and Deregulation Policies

In the overall context of the recent accent on strengthening the private sector's role in most Asian developing countries, the *privatization* of public enterprises (PE) has received growing attention particularly since the mid-1980s. The need for such a reorientation stemmed from a pervasive dissatisfaction with the performance of public enterprises, which in the early 1980s were estimated to account for over a quarter of gross fixed capital formation in all developing countries.

<sup>1</sup> Cf. G. P. Pfeiffermann, A. Madarassy: Trends in Private Investment in Developing Countries, 1990-91 edition, IFC Discussion Paper No. 11, January 1991.

<sup>2</sup> Cf. UNIDO: Foreign Direct Investment Flows to Developing Countries: Recent Trends, Major Determinants and Policy Implications, PPD. 167, 10 July 1990.

\* Both United Nations Industrial Development Organization (UNIDO), Vienna, Austria. The views expressed in this article are those of the authors and do not necessarily reflect the views of the UNIDO Secretariat.

Primarily driven by the need to lessen the fiscal burden which inefficient and loss-generating PEs had placed on state budgets, a great number of developing countries have embarked upon privatization programmes and policies albeit differing in scope, pace, methods and results.

In general terms, privatization is understood as the transfer of ownership and control of an enterprise or activity from the public to the private sector. Privatization or – as is mostly used synonymously – divestment thus comprises the outright or partial sale of state holdings to private sector interests as well as the contracting out or granting of operating concessions to private business including management, leasing and franchising arrangements. Moreover, the charging of market prices instead of fees for publicly supplied goods and services in a broader sense is sometimes being referred to as financial privatization. In turn, privatization is not to be equated with the concept of *deregulation* of an economy which encompasses the relaxation or removal of government regulations interfering with market forces, including constraints imposed upon competition against public enterprises. Yet, in order to reach its objectives, privatization would have to be closely co-ordinated with deregulation measures.

Whereas the relative importance attached to different approaches to privatization varies among Asian

**Table 2**  
**Inflows of Foreign Direct Investment to Developing Countries, by Region, 1980 - 1989**  
(percentage shares)

Host region	Average annual inflows		
	1980-1984	1985-1989	1988-1989
Africa	9.6	11.7	11.0
Latin America and Caribbean	48.8	37.4	34.2
Asia and Pacific	41.6	50.6	54.5
All developing countries	100	100	100

Source: Calculated from UNCTC: World Investment Report 1991, New York, July 1991, (Table 4).

developing countries, there are a number of common motives behind the increased involvement of private industry in areas hitherto reserved for public enterprises. These include:

- ☐ an increasing awareness of the general desirability of a more pronounced participation of the private sector in the development process;
- ☐ the financial strains stemming from large and persistent operational deficits of PEs, which have to be accommodated by public subsidies; and
- ☐ a growing discontent with the serious efficiency and productivity shortcomings recorded for the majority of PEs.

Before addressing some of the major problems and constraints encountered by recent privatization efforts in Asia, a brief review of the approaches adopted in selected developing countries of the region is given below.<sup>3</sup> As will be seen, the privatization issue is not only being addressed in the region's more advanced economies which have always strongly advocated the private sector's developmental role, but also in South Asia where public sector activities have traditionally been assigned important functions. Finally, initial moves towards opening the state sector to private business are also to be observed in several of the hitherto centrally planned economies of the region.

### Country Experience

Privatization efforts in the *Republic of Korea* have been regarded as a means to instil greater efficiency in loss-making PEs with a view to strengthening the industrial sector's overall performance. While the government in its development strategy in the 1960s and 1970s had attributed a strategic role to PEs, privatization was initiated with the divestment of Korean Air in 1969,

**Table 1**  
**Share of Private Investment in Total Investment, 1985 - 1989**  
(percentage)

Country	1985	1986	1987	1988	1989
Southeast and East Asia <sup>1</sup>	64.2	62.7	67.4	70.6	72.6
Fiji	67.0	67.3	69.9	60.2	56.6
Indonesia	47.6	52.2	52.3	54.2	59.2
Korea, Rep. of	73.8	74.6	78.9	80.5	81.3
Malaysia	47.0	40.7	48.8	62.2	64.4
Papua New Guinea	76.9	68.6	73.9	72.6	76.3
Philippines	75.5	75.2	77.4	77.2	78.3
Singapore	63.7	58.1	64.8	76.4	82.0
Thailand	61.9	64.7	73.3	81.2	83.0
South Asia <sup>1</sup>	49.1	47.3	48.3	50.6	50.1
Bangladesh	48.5	43.2	41.1	49.6	51.3
India	50.0	48.1	48.0	50.2	50.7
Nepal	61.3	58.3	60.6	56.4	44.2
Pakistan	41.6	41.2	40.6	41.9	43.6
Sri Lanka	44.1	45.7	51.1	55.0	60.9
Sample of 40 developing countries	53.2	53.3	55.3	57.1	58.4

<sup>1</sup>Simple (non-weighted) average.

Note: Averages have been recalculated.

Source: G. P. Pfeffermann, A. Madarassy: Trends in Private Investment in Developing Countries, 1990-91 edition, IFC Discussion Paper No. 11, January 1991.

<sup>3</sup> The following survey is partly based on ESCAP: Industrial Restructuring in Asia and the Pacific, Bangkok 1991, pp. 133-138.

followed only in 1982 by the sale of the national oil company, the conversion of the telecommunications authority into a publicly-held corporation and the privatization of all seven government-owned national commercial banks including the issuance of licences for more than fifty private finance institutions. Following the introduction in 1984 of several institutional measures to improve the PE's efficiency, in 1988 the government-owned steel company became the first (industrial) PE to be transferred through a series of share sales of PEs to the private sector. While strict bureaucratic controls have so far been maintained over the privatized commercial banks, the extension of the privatization programme accompanied by deregulation and liberalization measures is foreseen for the 1990s. The envisaged close co-ordination between government and private business in these efforts is a salient feature of the country's privatization approach.

In *Singapore*, the main objectives of the privatization policy embarked upon in 1984 have been (a) to reduce government involvement in industries in which private companies are able to operate competitively, (b) to expand the local stock market by selling PE shares to private business. As in the Republic of Korea, virtually all of the approximately 500 PEs either directly owned or controlled by the government in the mid-1980s were operating successfully. These companies were engaged in a broad range of activities, including large-scale manufacturing industries, oil refining, defence, transportation, the financial sector and housing. Following the sale of a 45 per cent minority stake of the largest state investment company in 1984 and the partial divestment of the national airline, the Public Sector Divestment Committee in 1987 recommended the gradual privatization of 41 PEs through the sale of shares as well as of 4 statutory bodies including the telecommunications authority. In implementing this recommendation the government has so far adopted a rather pragmatic approach, leaving at least minority stakes with the public sector in many cases. Also, by adopting a concept of "rolling privatization" (involving the channelling of funds from asset sales into new public ventures in technologically highly advanced areas) the government has underlined its ongoing commitment towards safeguarding the country's international competitiveness.

Since its inception in 1985 privatization policy in *Malaysia* has largely taken place on an ad-hoc basis resulting in the divestment of 26 PEs by 1990. According to the 1990 Privatization Master Plan, 50 out of a total of 900 PEs in a wide range of sectors with total assets estimated at M\$ 46 billion are now recommended for sale; another 99 loss-making PEs have been identified for restructuring

before divestment. Moreover, the government has been advised to sell off its majority stakes in 29 companies listed on the Kuala Lumpur Stock Exchange as well as its minority holdings in another 54 companies. However, whereas the national electricity board, the civil aviation department, the railways, and the postal services have recently been earmarked as potential privatization candidates by the government, in the past the state has retained a substantial share (referred to as "golden share") in most of the privatized companies, e. g. the national airline, the shipping company and the national car manufacturer. Basically, privatization efforts in *Malaysia* had been stimulated by the dismal performance of PEs which had surged in number under the New Economic Policy in force from 1970 to 1990 aiming at the redistribution of economic power in favour of the indigenous Malays. The new National Development Policy introduced in 1991 has reiterated the government's commitment to further privatization initiatives.

Inefficient state enterprises also marked the starting point for launching privatization in *Thailand* in the mid-1980s, when PE deficits totalled US \$1.7 billion, equalling 3.5 per cent of GDP. However, while the increased involvement of the private sector in infrastructure projects has materialized in a number of cases as announced (such as in highway construction, the new eastern seaport, telephone systems, or urban bus transport) privatization efforts in the majority of the 67 areas selected in the 1986 privatization programme seem to have come to a halt. This is attributed to the lack of attractiveness of loss-making PEs, complex legislative processes and strongly opposed trade unions.

Unlike her ASEAN partners, *Indonesia* up to now has not explicitly formulated a comprehensive privatization policy for the more than 500 PEs—200 thereof 100 per cent public—covering activities as diverse as petrochemicals, utilities, finance, transportation, communications, and major manufacturing sub-sectors. Rather, the policy pursued by decree since 1989 envisages privatization as one of several means of reorganizing the PE sector with a view to alleviating the strain on the state budget caused by inefficient entities. While the contracting out of customs inspection to a private foreign company in 1985 appears to have been the first and single most effective privatization measure, reservations have repeatedly been made regarding the transfer of PEs deemed strategic, such as the railways or the shipping line. Overall, the major thrust of government policies has been on a substantial deregulation of the economy, e. g. in foreign trade and banking, rather than on outright privatization.

In spite of the recommended privatization of 140 out of 296 PEs as identified by the Committee on Privatization

set up in late 1986, actual privatization in the *Philippines*, which was primarily targeted at reducing the fiscal burden caused by inefficient PEs, has remained far behind initial expectations. Thus by April 1988 only ten and by November 1989 only 30 out of 121 PEs decreed by the president for privatization had been sold, a consequence of strong resistance from key industries and large enterprises, but also of macroeconomic uncertainties and structural weaknesses, such as a thin capital market. However, with the divestment of a 30 per cent share of the Philippine National Bank in 1990 and the more recent sale of a large mining company, privatization appears to have regained momentum.

Privatization efforts in *Bangladesh* date back to the early 1970s when a number of small industries inherited by the state at independence were reprivatized. Under the "New Industrial Policy" promulgated in 1982 the list of industries reserved for the public sector was reduced to six: arms and ammunition, atomic energy, air transport, telecommunications, electricity and mechanized forest extraction. Consequently, within one year, 27 textiles mills and 33 jute mills – most of which had incurred losses – were divested, representing 38 per cent of the jute processing capacity, 45 per cent of the spinning capacity, and 57 per cent of the weaving capacity of the textile industry. Other privatization measures were directed at large-scale industries in chemicals, food, steel and engineering. Due to strong resistance from unions and workers the privatization programme came to a halt in 1984. Hence, a plan which foresaw the conversion of the public sector corporations into public limited companies and the sale of up to 49 per cent of the shares to the private sector was not implemented. With the "Revised Industrial Policy" of 1986, the scope for further privatization was broadened again leading to divestment of another eleven large enterprises by 1988. Overall, the privatization programme in Bangladesh, with more than 600 units affected, has been one of the largest in any developing country, yet its success has so far been limited. Numerous units were closed down soon after privatization, inter alia because of the high debts inherited and a refractory labour force resisting any staff reduction.

In *Pakistan*, after nationalizing numerous industries in the 1970s, efforts aimed at increasing the operational efficiency of PEs on the one hand and at divesting some of them to the private sector on the other have been made for many years. Thus, small-scale firms in cotton-ginning, rice-husking and flour-milling were reprivatized after 1977, as well as two larger firms – one engineering and one foundry company. When various measures taken in the early 1980s to improve the PEs' performance failed to reduce the widely incurred losses, the government

decided to divest 14 major PEs in chemicals, textiles, steel, automobiles, sugar and non-metallic mineral production. None of these units was actually privatized, however, partly as a result of private sector disinterest in acquiring loss-generating enterprises, problems related to potential labour lay-offs and the settlement of company debts as well as the thinness of the country's stock market. The present government, setting up a Privatization Commission in early 1991, has launched a new privatization initiative aimed at confining public sector investments to activities outside private sector interest or capability. Expressing a strong commitment to move ahead rapidly, it earmarked 115 PEs for full or partial divestment over a period of two to three years.

In *Nepal*, the history of government-endorsed privatization programmes dates back to the late 1970s; until now implementation of the various programmes has, however, fallen short of the declared targets. Within the government, a mixed attitude has prevailed with respect to the potential benefits of privatization which was considered to be in conflict with the basic needs planning approach and to lead to an excessive concentration of economic power in the hands of only a few private investors. Accordingly, most privatization offers were extended on the basis of only a partial (minority) transfer of ownership to the private sector which in turn showed a lukewarm response.

In the wake of significant economic reforms currently underway in *India*, in early 1991 the government embarked on a first step towards public-sector disinvestment by offering for sale up to 20 per cent of the equity in 31 profit-making companies active in utilities as well as in steel, engineering, petrochemical and fertilizer industries. So far bids have been invited only from several mutual funds and financial institutions indirectly controlled by the government. However, as in principle these institutions are free to resell the acquired companies to the public, this move does indicate a certain reorientation of the previous policy not to consider any privatization of PEs and rather to strive for more efficient management of PEs by enhancing their autonomy.

In the *Lao PDR*, a major economic strategy shift was initiated in 1985 with the so-called New Economic Mechanism which was followed by a number of further decrees covering, inter alia, privatization or divestiture of public enterprises. The privatization decree issued in March 1990 states that public sector disengagement is sought from "non-strategic" industries, i. e. excluding public utilities, banks and insurance, mining etc. Since mid-1989, the pace of privatization has significantly increased largely driven by the Prefecture of Vientiane as supervising agency of 70 mostly medium-scale

enterprises. In November 1989, half of the manufacturing companies (accounting for 35 per cent of all enterprises by number) had already been privatized and initial action had been taken on another 20 per cent. The approach adopted by the authorities has so far largely been on a case-by-case basis, i. e. not following any predetermined rules or guidelines. The relatively small size of companies offered as well as the inclusion of foreign investors, particularly Lao expatriates, have facilitated the programme's realization.

### **Privatization Obstacles**

Basically, there are two groups of privatization obstacles which, as in other developing regions, have also surfaced in Asia: implementation constraints and political constraints. As to the former, considerable managerial deficiencies within the state administration frequently prevail and are aggravated by overall structural weaknesses of the economy.

The administrative capacity to carry out multifaceted and often complicated tasks related to privatization measures has not been available in many cases. This applies to the issues of properly valuing the PEs' assets when determining or judging sale prices; the assessment of buyers' bids; the arrangement of ensuing finance and insurance; the complex legal issues involved; and frequently also includes the preparation of well-designed rehabilitation plans or the setting up of appropriate regulatory structures around the newly privatized firms. Furthermore, weak capital markets, particularly with respect to absent or poorly developed stock markets unable to absorb large divestments, continue to be a major structural impediment to privatization in many countries. In turn, private sector and local bank funds may not suffice to finance purchases of PEs which often are among the largest companies in a country. In fact, experience shows that the more developed a country's capital market, the easier it is to find suitable investors for PEs to be privatized.

The scarcity of PE managers familiar with providing corporate leadership and direction when obliged to act in a more market-driven environment is another typical structural weakness. Also, potential private investors who for whatever reason lack confidence in a government's privatization policy can only be expected to step in at a later stage. In this context, given the predisposition of many countries to primarily sell off hitherto unprofitable PEs, the cautious private sector response has come as no surprise.

Concerning political constraints to privatization policies, it is obvious that the immediate potential losers generally utter their strong opposition. Thus labour groups

or unions afraid of both substantial lay-offs at privatized companies and a subsequent loss of political influence tend to offer strong resistance. The same applies to the management of the concerned PEs and the corresponding line ministries unwilling to relinquish long-standing vested interests. Finally, in some countries a delicate social balance safeguarding the relative positions of certain economic groups also places limits on the scope for privatization.

As has been shown, the sometimes ambitious privatization programmes have materialized to a limited extent only. Furthermore, it needs to be pointed out that privatization of PEs does not on its own bring about increased efficiency and profitability. To reach its objectives, privatization has to go hand in hand with a strengthening of market forces through carefully designed deregulation and liberalization moves. For instance, divesting a PE enjoying a monopoly position without ensuring free market access for other companies or introducing anti-monopoly legislation is clearly self-defeating. Privatization is but one facet of the larger policy issues of private sector development; by itself it does not constitute a sufficient condition for an increased role by the private sector in economic development.

### **New Role of Governments**

The above brief overview of privatization approaches pursued in selected Asian developing countries confirms that the issue ranks high on the present policy agenda. At the same time, it demonstrates that in most cases privatization initiatives have not always met the initial high expectations placed on them.

Notwithstanding the slow progress made in many of the privatization programmes, it is clear, however, that in most countries of the region the private sector is regarded as the key engine of growth and will play the lead role in industrial development in the future. In the course of time, the share of production and investment originating from public industries can be expected to decline further as a result of the dynamism unleashed in a private sector less stifled by bureaucratic restrictions than in the past.

This implies a changing private-public sector relationship away from the traditional top-down approach towards greater co-operation and co-ordination. Private companies themselves will increasingly have to articulate the requirements for government support, be it in terms of policy frameworks, incentives schemes or financial assistance. Also, with the reduction of government involvement in the financial sector, there will be an enhanced role by private banks and other financial institutions in promoting industrial development.

At the same time, the increased role of the private sector in industrial development does not imply that government policy is becoming redundant or is becoming less important than in the past. On the contrary, a strong and efficient government capable of designing, implementing and enforcing a consistent set of industrial policies is a *sine qua non* if the private sector is to prosper in a stable framework. Reliance on markets, competition and private initiative is not to be equated with a "laissez-faire" economy.

A number of government functions have traditionally been generally accepted. First, these relate to instances in which markets cannot function as a result of market failures occurring systematically.<sup>4</sup> Typical examples are externalities as well as natural monopolies. In the case of externalities – external costs or external savings – a third party not involved in an economic activity is affected by it leading to a divergence between private and social costs and benefits. For instance, goods involving external costs, such as environmental pollution, tend to be overproduced from a social point of view. Natural monopolies may arise from increasing returns to scale (applying to many public utilities) thus excluding fair competition.

Secondly, governments must provide so-called public goods, i. e. those goods available for general consumption, and are generally expected to provide so-called merit goods, i. e. goods which individuals do not demand at socially desirable levels when left to the free market (e. g. health; basic education).

Accordingly, the classic government functions encompass the creation of the *physical* infrastructure (transportation; power and water supply; communication) for industrial development which has proven to be of critical importance, inter alia, for the locational pattern of industry and thus the degree of regional disparities. This does not imply, however, that there is no room for the private sector in the provision of infrastructural services. In many cases, public goods (e. g. telecommunication and transport services, including roads and railways) can be and actually have been commercialized. For instance, in Thailand the private sector has recently become involved in unconventional activities such as the selling and full development of land for industrial estates (which are subsequently taken over and operated by the Industrial Estates Authority of Thailand); the construction and operation of the large-scale Bangkok expressway project; and the private management of a number of container ports. In such cases, it remains the government's central

task to ensure that the potential monopoly power associated with the allocation of large-scale infrastructural projects/services to private companies is effectively controlled.

### Building up National Competitiveness

It is increasingly being recognized, however, that the role of governments in promoting industrial development is going beyond the areas outlined above. Governments – in addition to creating the required infrastructure and a stable macro-economic framework through appropriate monetary and fiscal policies – can make critical contributions to stimulating technological innovation and enhancing industrial efficiency and competitiveness. Indeed, international competitiveness is no longer just a micro-level phenomenon; today it is as much determined at the national level as it is at the company level. "In a world of increasingly global competition, nations have become more, not less important. As the basis of competition has shifted more and more to the creation and assimilation of knowledge, the role of the nation has grown."<sup>5</sup> A whole national economy can be regarded as a "unit" in competition with other economies in the international market. Therefore, national competitiveness needs also to be seen in a longer-term perspective, as the competition of entire economic and social *systems*. In the long run, the development strength of an economy would depend upon the ability of its productive sectors to dynamically develop and secure *future* competitiveness and thus *future* increases in real wages and living standards of the population.

In general, governments are no longer – if they ever were – in a position to design a single national economic strategy and push it through in a top-down approach by picking "winners" or "strategic industries". Instead, they need to develop an overall strategic "vision" of building up national competitive strength and to establish the conditions under which synergy effects can be achieved in the strategies pursued by various actors: companies, industrial associations, trade unions, support institutions, banks, etc. In other words: the process of industrial strategy formulation by governments is moving "upstream" to synchronize and support a multitude of existing strategies rather than to impose a unified final design. Therefore, assigning to the private sector a lead role in industrial development must not be seen as requiring a "minimal state". Rather, it presupposes an efficient and competent government machinery with highly qualified staff capable of working closely with the private sector.

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<sup>4</sup> Cf. UNDP: Private Sector Development for Promoting Economic Growth in Developing Countries of Asia, April 1988.

<sup>5</sup> M. E. Porter: The Competitive Advantage of Nations, in: Harvard Business Review, March-April 1990, p. 73.

To give but one of many possible examples: with the general relaxation of foreign investment rules, the function of national investment agencies has become less regulatory and is now increasingly geared to promotional and supporting activities. In many countries, investment agencies are undertaking efforts to integrate foreign investors more strongly into the national economy, e. g. through linking them up with domestic companies with a view to increasing the local content of production. Thailand's Board of Investment (BOI) is a case in point. In early 1992, the BOI launched an initiative to establish so-called "investors clubs" for export-oriented manufacturers seeking Thai sub-contractors to supply parts and components. The BOI serves as a matchmaker which in specified industrial branches – starting with the electronics and the machinery industry – brings together interested companies and also seeks to stimulate a pooling of resources of small domestic companies so that they can meet the demands of large foreign firms. The overall objective of this BOI programme is to counteract the country's eroding competitiveness as a low-cost manufacturing base and to create new system advantages in terms of integrated production structures.

### Response from International Organizations

International organizations active in the field of industrial co-operation are facing a situation of the private sector being the dominant economic force in most of the Asian region's countries. In others, a transition towards market-based development and a greater private sector involvement is underway. This is a trend which has been advocated and supported by most international organizations. Now strategies and programmes of the international organizations themselves are called for as to how they can respond most effectively and mobilize their resources for the benefit of the private sector. Indeed, both the actual areas of co-operation and the nature and form of the services offered will need to be adapted to the requirements of the final user – private industry. This means not only that private industry will have to play a major role in identifying and formulating the actual assistance requirements, but that the services will have to be provided directly and speedily to the industrial entities according to the terms and conditions prevailing in the private sector.

In this context, a number of issues arise for international organizations:

- ☐ First, what are the most essential areas for technical assistance to private industry?
- ☐ Second, how can it be assured that the technical assistance is carried out in conformity with the market and

no distortions are created in terms of selection of recipients, costing of services and competition with commercial entities?

- ☐ Third, what are the most suitable modalities, including financing schemes, for assistance to private industry?

The following sections intend to provide a basis for discussion of these issues, inter alia by drawing on UNIDO's recent experience in co-operation with private industry.

### Technical Assistance to Governments

Three different levels can be distinguished at which international organizations can make contributions to strengthening the role of the private sector in industrial development: (1) the overall policy level, (2) the institutional level and (3) the company level.

(1) To start with, international organizations can provide essential analytical inputs and advisory services to governments that have embarked upon privatization and/or deregulation programmes. While it will remain the governments' prerogative to decide about the objectives, pace and priority areas of privatization efforts, they could no doubt benefit from impartial advice and assistance in designing consistent privatization policies and measures and in translating these into concrete implementation approaches. Some crucial areas for such assistance would include:<sup>6</sup>

- ☐ *Human resource development:* This involves the training of government staff in the mechanics of privatization, including reorganization techniques, methods of company valuation, formation of joint ventures, offer of shares in the market, underwriting etc. It also refers to training for public-sector managers in operating companies under the pressure of competition, with special emphasis on marketing and financial management training.

- ☐ *Financing:* The development of capital markets is of critical importance in the more advanced countries of the region and the Asian Development Bank is very active in this field. Above all in the LDCs, development finance institutions (DFIs) would have to be key actors in view of the shortage of indigenous entrepreneurs with sufficient financial resources to take over large public enterprises. In LDCs, therefore, most enterprises intended to be privatized will have to be joint ventures – involving foreign private investors and/or domestic or foreign DFIs. International organizations can act as a broker to bring about such arrangements.

- ☐ *Rehabilitation:* Assessing the rehabilitation/modernization requirements (including related feasibility



studies) of companies to be privatized could effectively accelerate the privatization process in many countries. Such pre-privatization company audits – to be carried out by neutral analysts – would be a critical input for take-over decisions by interested private investors. They could establish which specific action is required and at what cost to secure the long-term viability of individual companies.

At present, a number of international organizations are actively supporting ongoing privatization and deregulation programmes. This includes both financial assistance provided by the World Bank and the Asian Development Bank in the framework of Industrial Sector Programme Loans and technical assistance as provided by UNDP (within their Interregional Network on Privatization established in 1988), UNIDO and other organizations.

### Help with Institution-building

(2) At the institutional level, international organizations – drawing on their experience in a multitude of countries in different regions and at different levels of development – can assist in building up efficient forms of private industry representation and organization. Particularly in LDCs where such institutions are often lacking or malfunctioning, industrial associations such as Chambers of Industry and Commerce need to be established and typically need some seed funds as well as expert advice and operational support in the initial stage. The existence of efficient industry associations is essential for various reasons, including (i) to deliver services to member companies, (ii) to act as representatives of private industry in policy dialogues and negotiations with the government and (iii) to function as counterparts for technical assistance and other promotional programmes by international organizations. In a way, therefore, in many countries the latter are facing the challenge of first having to create the institutional conditions under which technical assistance can subsequently be delivered to private industry.

It is crucial, however, that international organizations work out modalities to co-operate with private industry without compromising their own impartiality and without distorting competition. Implementing projects together with industry associations would seem to be a logical approach to ensure that these objectives are met by spreading the benefits derived from assistance projects to a wide range of industrial companies. For instance, in Thailand UNIDO is implementing projects with the Federation of Thai Industries as counterpart in which

sophisticated testing services as well as plant-level advice on “best manufacturing practices” are available upon request to all private companies in specific branches.

### Company-level Assistance

(3) Finally, international organizations in principle can also work directly with private manufacturing companies through providing plant-level assistance. So far, UNIDO is unique among the UN agencies in this respect based on its mandate directly to support “industrialization in the public, co-operative and private sectors”. Since 1986, UNIDO has extended its services to numerous private industrial enterprises in Asia and the Pacific as well as in other developing regions. Such services – which are rendered within the context of so-called special trust fund agreements<sup>7</sup> – encompass the full range of UNIDO activities, inter alia including:

- ☐ diagnostic and advisory services on technical, organizational, financial, marketing and management issues in the context of modernization or rehabilitation programmes;
- ☐ environment and energy audits and advisory services;
- ☐ project evaluation, opportunity studies and full-fledged feasibility studies;
- ☐ investment promotion, including the establishment of links with foreign investors;
- ☐ procurement advice and services;
- ☐ training of technical and managerial staff;
- ☐ advisory services for production networking, including domestic and international sub-contracting, as well as other forms of international enterprise-to-enterprise co-operation such as the formation of R&D consortia or joint marketing arrangements.

In general, these services are not different from those provided to public sector enterprises in the past. However, in the case of private companies specific issues arise concerning the modalities and financing of technical assistance.

Generally, private companies operating in highly competitive markets require a speedy delivery of highly specialized and flexible assistance inputs. However, “quick response” has not been a major strength of international organizations in the past and therefore adjustments are necessary in the administrative procedures which were primarily geared to large-scale and long-term assistance projects serving government institutions. Mechanisms will have to be devised which ensure government endorsement and UNDP coordination

<sup>6</sup> Cf. UNIDO: Privatization Theory and Policy, IPCT. 156 (SPEC.), 16 April 1992; UNDP: Guidelines on Privatization, New York 1991.

<sup>7</sup> These can be either self-financed (in which case a private company pays UNIDO for its service) or third-party financed.

of assistance to private companies without subjecting it to complex and time-consuming bureaucratic processes.

As mentioned above, when implementing projects directly benefiting private industrial companies, international organizations must ensure that no market distortions are created. Therefore, the full costs for company-level services should be borne by the recipient enterprises which will increase their efficiency and profitability as a result of the specific assistance provided.

A further aspect in this context refers to potential competition between international organizations and domestic consultancy companies. The former—given their special reputation and mandate as unbiased neutral advisers—should not act as just another consulting firm.

First, they should concentrate on particularly demanding segments of consultancy services requiring sophisticated international expertise and access to multilateral information networks. Complex procurement services or feasibility studies involving international market assessments would be cases in point. Second, within their advisory services to the private sector, international organizations should seek to involve, to the maximum extent possible, existing domestic consultancy firms, e. g. through sub-contracting arrangements thereby extending support and training to their further development. In the case of large-scale projects, it would also appear appropriate to cooperate with big international consulting firms—a model that could be referred to as “co-consulting” in analogy with the co-financing of development projects.

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Ramesh C. Garg\*

## The Case for Debt-forgiveness for Latin America and the Caribbean Countries

*Resource transfer to Latin America and the Caribbean was negative throughout the eighties. Debt-forgiveness would benefit not only the debtor countries, however. Lending countries and institutions would also stand to gain.*

The “debt crisis” still overshadows the horizon of international financial markets. It has been causing political instability and the collapse of the economies of several Latin American countries. The debt crisis has resulted in inhibiting the transfer of capital and investments from developed countries to the debt-ridden less developed countries (LDCs). At the same time, the stocks of several private international banks are under severe pressure and selling substantially below their book values due to their exposure to LDC debt, particularly in Latin America. Various proposals have emerged for finding a satisfactory resolution of the debt problem, yet the progress to date in reducing the debt burden has been very slow.<sup>1</sup> According to World Bank estimates, the outstanding debt of all developing countries amounts to

\$ 1.35 trillion at the end of 1991, which is unchanged from 1990's total.<sup>2</sup> A significant portion of this debt is owed to private banks. A number of Latin American countries have instituted debt-equity swap programmes, which have made a small dent in the growth of external public debt<sup>3</sup> for the Latin American and the Caribbean countries. According to the World Bank statistics, the external public debt of Latin America and the Caribbean countries

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<sup>1</sup> Cf. Ramesh C. Garg: Exploring Solutions to the LDC Debt Crisis, in: The Bankers Magazine, January/February 1989, pp. 46-51; Steven Miller: Coping With The LDC Debt Crisis, in: The Bankers Magazine, May/June 1988, pp. 29-33.

<sup>2</sup> Eduardo Lachica: World Bank Issues Warning on Debt Woes, in: The Wall Street Journal, December 16, 1991, p. A9A.

<sup>3</sup> External public debt is defined as the debt incurred or guaranteed by government repayable to non-residents in foreign currency, with an original maturity of more than one year. In the paper, wherever the term “debt” is used, it refers only to the external public debt and does not include the private external debt.

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\* Eastern Michigan University, Ypsilanti, Michigan, USA.