PRIVATIZATION IN NIGERIA: OPTIONS FOR THE NEXT MILLENNIUM

BY
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1.0 INTRODUCTION

The world is changing, and with it our ideas about the role of the state in economic and social development. Today's intense focus on the state's role is reminiscent of an earlier era, when the world was emerging from the revenges of World War II, and much of the developing world was just gaining its independence. Then development seemed a more easily surmountable (and largely technical) challenge. Good advisers and technical experts would formulate good policies, which good governments would then implement for the good of society. State-led intervention emphasized market failures and accorded the state a central role in correcting them. However, the institutional assumptions implicit in this world view were, as we all realize today, too simplistic. Flexibility to implement the policies devised by technocrats was accorded pride of place, accountability through checks and balances was regarded as an encumbrance.

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In a few countries, things have indeed worked out more or less as the technocrats expected. But in many countries, outcomes were very different. Government embarked on fanciful schemes. Private investors, lacking confidence in public policies or in the steadfastness of leaders held back. Powerful rulers acted arbitrarily. Corruption became endemic. Development faltered, and poverty endured. Over the last century the size and scope of government have expanded enormously. The pre-World War II expansion was driven by, among other factors, the need to address the heavy toll on economic and social system brought by the Great Depression. Industrial economies expanded the welfare state, and much of the developing world embraced state - dominated development strategies. The result was a tremendous expansion in the size of government worldwide.

In the 1950s, the government of many developing countries were actively involved in ownership and management of companies. Many economic planners had recommended state ownership as an effective alternative to the free enterprise system to stimulate economic growth. Following independence, most Less Developed countries embarked on development strategies that included government ownership of enterprises, apart from its usual presence in utilities (gas, water and electricity), transportation (railroads, airlines, etc.) and communications. In countries like India, Mexico and Nicaragua, public enterprise accounted for 80 per cent or more of the value added in manufacturing (World Development Report, 1983).

Nigeria was no exception in terms of the belief that the state and public enterprises have a role to play in the country's development efforts, the government in conjunction with the Private sector, mostly foreign, directly involved in areas ranging from the production of foodstuffs to assembling cars. The oil boom of the 1970s enabled the Government to venture into "Ownership" and control of economic activities. The Nigerian Enterprises Promotion Decree of 1972 set the basis for the Government's extensive participation in the ownership and management of banking, insurance, and industry. The public sector played a dominant role in the economy, accounting for almost half of the GDP and two-thirds of modern sector employment in the 1970s. By 1980, there were about 70 non-commercial Federal parastatals. There were also large numbers at the State level.

However, by the early 1980s economic results showed that

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State Capitalism had failed to achieve its objectives. The deregulation movement set in motion by the Reagan Administration in the United States appears to have started a global trend of restoring the free enterprise spirit. In Britain, the Thatcher Government privatized some of its huge government corporations including British Gas, British Telecom and British Airways (Redwood, 1987; Abromeif, 1989). Privatization has also taken place in other Western European countries (**Vickers and Wright**, 1988). In Italy, as a result of changes in economic policy, the state-owned IRI group of companies was opened for privatization. The IRI formula was used to increase private shareholding as part of a financial strategy to rationalize the business portfolio (corrias, 1990). In the Eastern European Countries and Russia, there is a total shift in ideological orientation from Socialism/Communism to market oriented system. Consequently, many establishment formerly owned and managed exclusively by the State have either been commercialized or Privatized or are in the process of being privatized. In Asia, after forty years of Socialism, India has begun to restore the free enterprise System by removing many restrictions. The people's Republic of China has opened its doors to the outside world and seeks joint ventures with privately-owned foreign companies. It now allows private ownership of business by its citizens (Liu, 1997).

As in the 1940s, the renewed focus on the role of the state today, has been provoked basically by the dramatic events in the global economy, which has fundamentally changed the environment in which states operate. The global integration of economies and the spread of democracy have narrowed the scope for arbitrary and capricious behaviour. Taxes, investment rules, and economic policies must be ever more responsive to the parameters of a globalized world economy. Technological change has opened new opportunities for unbundling services and allowing a larger role for markets. These changes have meant new and different role for government, no longer as sole provider, but as facilitator and regulator. (**World Development Report, 1997**).

When the Nigerian economy entered a recessionary phase in the 1980s, it was argued by policy makers that government or public enterprises must operate according to the profit motive rule. Hence, the structural adjustment programme of the Government set in motion a process for privatizing and commercializing public enterprises. Although this programme has been implemented to a reasonable extent, it does appear that the government lacks the will to pursue the remaining aspect of the programme. This paper seeks to discuss issues in privatization in Nigeria with a view to proffering policy options for the new millennium. Accordingly, the remaining part of the paper is divided into four sections. Section II discuses theoretical issues, Section III examines Privatization of the public Enterprises in Nigeria. Section IV contain policy options for the new millennium. The study is summarized and concluded in Section V.

2.0 PRIVATIZATION: Theoretical Issues

Privatization can be defined as the systematic transfer of appropriate functions, activities or property from the public to the private sector, where services (production and consumption) can be regulated more efficiently by the market and price mechanism. The end product of privatization is thus a significant change in the relationships between the government and the private sector, with the role or the level of involvement of the state in the economy being reduced, as more of the functions get shifted to the private sector (Kay and Thompson, 1986). Such a reduction in the level of state involvement will in turn relieve the state not only of the burden of running the enterprises, but also remove the accompanying budgetary obligation (especially where some of the enterprises are making losses). Furthermore, once enterprises are privatized they get exposed to competition as the environment within which they operate changes significantly.

The enterprises are made to face a different set of constraints, requiring a reorganization of their objectives and incentive structures to be in line with those faced by their competitors. In addition, the threat of bankruptcy becomes very real.

At the theoretical front, there are two major lines of argument in favour of privatization. The efficiency and the fiscal arguments. The case for public ownership has traditionally rested on considerations of allocative efficiency. That is, in the event of the market mechanisms failing to produce efficient outcomes, public ownership may be the solution. In contrast, the case for privatization basically rests on the incentives and constraints that the market provides to promote efficiency within the firm - that is 'technical'

efficiency. The former is based on the tacit assumption that productive efficiency will be satisfied irrespective of the conditions of ownership or competition. The validity of this assumption is however restrictive:

(i) Allocative efficiency will be violated in the absence of technical or productive efficiency. Thus, productive efficiency is a necessary condition for allocative efficiency, while the converse is not necessarily true;

(ii) There is a perception that public enterprises do not behave in a cost-minimizing manner for a variety of reasons. First, public enterprises, unlike private enterprises, do not have a clear profit objective and in the absence of profit motive, there is no incentive to minimize costs.

The latter is reinforced by the absence of the threat of bankruptcy as the government is always there to bail out the public enterprises in the event of financial crisis (Domberger and Piggott, 1986). The second problem of public enterprises is their openness to manipulation by politicians who may set non-commercial objectives for the enterprises in pursuit of their political agenda. Such political interference can be extremely counter productive, and can lead to gross inefficiency. Third, the incentive structure confronting public sector management is often not compatible with the pursuit of productive efficiency, since typically, neither their earnings nor tenure are directly linked to any measure of performance. In addition, public enterprise managers usually escape the discipline of financial markets, including the threat of take-over. For political and social reasons, public enterprises are seldom liquidated. Instead, they are cushioned by soft budget constraints and preferential access to both domestic and foreign credit (Galal, 1990). Furthermore, trade unions in general, and public sector unions in particular, can be expected to put up stiff opposition whenever new working practices are proposed which, while enhancing efficiency, might also contribute to job losses. Such a stance by public sector unions has often been supported by government as a consequence of their sensitivity to the unemployment issue. As a result, public enterprises do not only suffer from overcapitalization, but also suffer from over-staffing making most of them to persistently deviate from the two key requirements for productive efficiency - that is, that the minimum quantity of any input to be used to produce a given level of output, holding all other input levels fixed, and the requirement that inputs should be used in a cost-minimizing combination, which can only be determined by reference to relative factor price (Domberger and Piggott, 1986).

Advocates of privatization argue that the process restores incentives that promote productive efficiency. The threat of bankruptcy - which may be regarded as the ultimate sanction on inefficiency - is perhaps the most important. In addition, private ownership in principle, frees enterprises and their management from political interference in the decision making process. By the same token, private ownership takes away the advantage of preferential access to credit which the enterprise might have enjoyed under the public ownership.

However, Kay and Thompson (1986) stressed that privatization on its own is not a necessary and sufficient condition that guarantees maximum productive efficiency. The efficiency gains can be blunted by the lack of competition in the product markets and the separation or divorce of management from ownership typical of large corporations. The satisfying behaviour of hired management becomes ever more problematic when privatized firms have dominant positions, which make them potentially profitable, and where management discretion to pursue less than maximum efficiency is greatest. Under such circumstances, the threat of bankruptcy becomes minimal. This leaves the threat of takeover, which exists under private as opposed to public ownership, as the only constraint on the satisfying behaviour or "managerial slack". When owners are dissatisfied with the manner in which their enterprises are managed, they will dispose of their shares, and as shares get sold the valuation ratio (the ratio of the firm's stock market Value to its accounting Value) of the firm will drop, thus increasing the probability of takeover. In this way, private ownership and the capital market impose a constraint on the management's satisfying behaviour (Domberger and Piggott, 1986; Galal, 1990; and Truu, 1992).

Competition in the product market and capital market pressures thus enhance productive efficiency within privately owned enterprises. For its part, competition punishes

persistent under - performance by making the threat of bankruptcy real, while capital market pressures ensure that if management is not successful in averting a downward performance trend, it will be displaced through takeover long before the firm has reached the point of no return. Privatization or divesture thus internalizes the benefits from and the cost of ownership. It substitutes interested owners, for uninterested bureaucrats, thus motivating the new owners to devise more effective mechanisms to ensure the profitability and to maintain the long-term Value of their firm (Galal, 1990).

In a large majority of countries where privatization has been implemented, the need to ease the fiscal burden imposed by public enterprises or to generate revenue to finance the deficits has been cited as a major justification. Most often, the need to privatize state-owned enterprises arises from the conflicts between expanding demands for government expenditure on the one hand, and of restricting the tax burden on the other.

State enterprises, privatization, and fiscal policy interact in various ways. On one hand, losses by state enterprises are part of the fiscal problem and fiscal crisis push privatization toward the top of the policy agenda. Moreover, fiscal crisis itself usually impedes attempts to control state enterprises and their losses by weakening the state's administrative and monitoring capacities, strengthening centrifugal tendencies within the state and exacerbating bureaucratic conflict. Lastly, investment by state enterprises is a prime target for budget cuts and without investment the quality of products, infrastructure, and services quickly deteriorates. These tarnish the image of the enterprises and increase public support for reform and privatization. A fiscal crisis is a major determinant of, if not a necessary condition for the decision to privatize (Pinhero and Schneider, 1995).

On the other hand, privatization is perceived to be part of the fiscal solution. The proceeds from enterprise sales can be treated as capital revenue or loan repayment in the government accounts, which will lead to a once-and-for-all reduction in the fiscal deficit, assuming that the sale price obtained is greater than the net income generated for the government by the enterprise in the year of the sale. The change in the deficit, however, may not necessarily reflect a fundamental change in the fiscal policy stance. To gauge such a change, an analysis of the income flows and changes in the government's net worth arising from privatization is necessary (Hemming and Miranda, 1991).

The fiscal impact of privatization thus, depends on a number of factors. It depends on the value of the assets sold, productivity changes resulting from the transfer of ownership, and the way the government uses the proceeds from the sale of the public assets. The sale of public enterprises does not always lead to revenue gains to the state. For example, consider a simple case where the price paid by the buyers for an enterprise is equal to the discounted stream on net revenues the government would receive under public ownership. If the change in ownership leaves efficiency, profitability and income taxes unaffected, and if the public enterprise imposes no burden on the government budget, then privatization would simply change the government's liquidity position, but not its wealth. Instead, the government would have substituted liquid assets for equity. Under those circumstances, privatization would have no impact on the fiscal budget in the long-run.

There are, however, instances where the neutrality of divestiture do not hold. First, when buyers expect that they can improve the profitability of the enterprise, they may be willing to pay a price higher than the discounted stream of profits that the enterprise would have received under continued public ownership. The second instance relates to enterprises that make losses, and thus impose a financial burden on the government. Third, in the event of a government faced with fiscal imbalances there may be pressure on it to use the proceeds to retire some of the debt to reduce budget deficit (Galal, 1990). Privatization will thus have a favourable effect on the fiscal budget where one or more of these conditions are obtained. However, these expectations may not materialize. The government may fail to secure a price that exceeds what the Treasury would receive under continued public ownership. Moreover, productivity and profitability gains may not be reached if the privatized firm operates in a monopolistic set up. However, privatization coupled with deregulation may be in direct conflict with the objective of maximizing the sale value of the public enterprise. The expected profitability of a privatized enterprise is likely to decrease with the reduction in or the elimination of barrier's to entry (Domberger and

Piggott, 1986). A protected monopoly is likely to attract more buyers and generate higher revenue than an enterprise that either faces actual or potential competition. If the government continues to protect the enterprise subsequent to privatization, some of the economic gains of privatization may never materialize.

Most social analyses gloss over the revenue benefits of privatization which should not, in their opinion, be a primary objective. For instance, World Bank (1992) opined that "the economic benefits of privatization are maximized when governments make improved efficiency the number one goal". Thus, maximization of revenue should not be the primary consideration. Indeed, both the IMF and the World Bank are unambiguous in down-playing the fiscal benefits of privatization, even though their debtor governments adopt the policy to demonstrate their commitment to stabilization (see World Bank, 1992; Heller, 1990; Mansour, 1988).

3.0 PRIVATIZATION OF THE PUBLIC ENTERPRISES IN NIGERIA

One of the major elements of Nigeria's structural adjustment programme (SAP) was the encouragement to rationalize and privatize public sector enterprises. The public enterprises sector consist of about 100 enterprises at federal level. These enterprises are spread over agriculture, mining, manufacturing, transport, commercial and other services activities. As at 1986, government investment in this sector was over N23 billion (N8 billion in equity and N15 billion in loans). According to the Government, the annual returns are less than N500 million. Under Structural Adjustment, public enterprises were classified into five broad categories; those which are to be:

a) fully privatized;
b) partially privatized;
c) fully commercialized;
d) partially commercialized;
e) public institutions.

The Privatization and Commercialization Decree No. 25 of 1988 earmarked sixty-seven companies for full privatization, eleven for full commercialization, fourteen others for partial commercialization and forty-three for partial privatization.

The Technical Committee on Privatization and Commercialization (TCPC) became effective in 1989. In 1992, the Programme of Privatization and Commercialization was modified slightly. The Federal Government reversed the earlier policy of maintaining its holdings in commercial banks and decided to offer its equity investments in these banks to the public. By the end of 1992, a total of 1.12 billion shares with a market capitalization of N4.73 billion was offered for sale to the Nigerian public.

In the 1991 budget speech the then President noted: "It is gratifying to note that the vast majority of those who purchase shares of privatized enterprises were in fact low-income people, who also purchases the bulk of the share offered for sale"

The above statement is contentious, in the first instance what percentage of the total shares is owned by low income earners? What about the almost 60 - 70 per cent of Nigerians who live in the rural areas and have no access to such facilities? In any case, as a result of rapidly declining real wages, most low-income workers do not even have enough for the basic necessity of life let alone acquiring shares. Consequently, to conclude that ownership of shares is being liberalized is not correct. For several reasons including political and selfish interest, the privatization of key public utilities in Nigeria appear to have lost steam between 1991 and date. However, in 1997 the Federal Government admitted that, for over 20 years, government has been investing in projects that were exclusively meant for the private sector. These investments were in the form of loans from multilateral institutions, the international capital market, as well as internally generated revenue. The door was shut to private foreign investments. The anticipated improvement in living standard in 1997 can only be realized with growth through investments. In view of the relative dearth of investment resources in the country, it is imperative that every step be taken to improve the resource mobilization and resource utilization. The government further noted that in view of the problems of Management and efficiency of key public enterprises, government has in the past few years considered the desirability of commercialization and privatization of some of these enterprises. During 1997 the ground work previously started will continue and a wide range of consultation will be undertaken. Government is interested to ensure effective and efficient management of these enterprise and the nation gets maximum benefit in the form of management and resources.. (FGN, 1997).

Despite the above announced policy intent by government in 1997, the expected groundwork for privatization did not materialize. Consequently, the government further articulated its position on this issue in the succeeding year thus:

Government has now resolved to commence the privatization of public enterprises in 1998 in line with the vision 2010 programme. Government desire is to ensure effective and efficient management of public enterprises so that the nation can get maximum benefits from the resources so committed. Government is aware of the anxiety that the privatization exercise has generated and is determined to ensure that the gains of the exercise for Nigerians as a whole outweigh whatever losses may occur.

In particular, the government declared that she intended to use the privatization programme to develope a wider business ownership and stimulate the competition necessary to ensure efficiency in the system. Consequently, the government adopted the guided privatization approach. This involves privatizing one enterprise at a time so that the lessons of experience will be used to improve upon the programme.

In practical terms, the government indicated that she will invite some core/strategic investors with the relevant expertise, particularly technological and managerial capability, to participate in the ownership of the enterprise with a specific shareholding. Government was to retain 40% of equity in the enterprise to be privatize, while 20% of the shares were to be sold to Nigerians. Furthermore, the government categorically stated that "government enterprises in telecommunications, electricity, Petroleum refining, Petro-Chemicals, coal and bitumen production, and tourism development, will be privatized in the first phase of the programme. (FGN, 1998)

In the 1999 budget, the government admitted that NEPA could not be preferred for privatization in 1998 as proposals on how this integrated monopoly is to be broken up into its constituent functional entities (generation, transmission and distribution) and the new laws and regulations (including a regulatory commission) for the sector are being examined (FGN, 1999).

From the above account, it is clear that in Nigeria, for the past three to four consecutive years, the government has not been able to executive the programme largely as a result of conflicting interests and lack of consensus on how to carry out the programme without jeopardizing the welfare of the citizenry. In the next segment, we shall articulate the various options.

4.0 OPTIONS FOR THE NEW MILLENNIUM

Interest has revived in finding ways for the government to work with the private sector in support of economic development, and to provide regulatory framework supportive of competitive markets. Yet in most countries, state and market remain fundamentally at odds. Private initiatives is still held hostage to a legacy of antagonistic relations with the state. Rigid regulations inhibit private initiative. And state enterprise, often buttressed by monopoly privileges, dominate economic terrain that could more fruitfully be given to our competitive markets. At the extreme, a mass of inefficient state enterprises block private dynamism entirely, even as it imposes an unmanageable fiscal and administrative burden on the rest of the public sector.

Because privatization typically involves a fundamental shift of economic power, it produces political conflict, often assumes the characteristics of a zero-sum game, and sometimes involves such intense debate that, for the policy maker, the perceived political costs of privatization can outweigh the expected economic benefits at the face value. The main issue has thus boiled down to what strategy to adopt for the achievement of this laudable aim. It is in the light of the above impasse that we proceed to enumerate the options to be adopted by the government to achieve the twin objective of efficiency and welfare maximization, without necessarily transferring the wealth of the country to a few individuals who most often became rich at the expense of the state.

The need to privatize rapidly a large number of state-owned enterprises (SOEs) in an equitable manner led to the development of voucher-based mass privatization programmes throughout Eastern Europe, Central Asia, and the former Soviet Union. Non-Voucher variations of these programmes, which collectively pool equity distributed to citizens, have emerged within the context of privatization in countries as diverse as Boliva and the Zambia. Many other countries have made use of discounted public offerings to elicit worker participation in privatization, or to distribute widely ownership of privatized equity. These three basic techniques of achieving broad based ownership: Voucher-based programmes; collective investment programmes

and public offering, offer social and political advantages over more traditional privatization methods.

In Nigeria, public offerings have been used extensively in the implementation of the privatization programme. Consequently, we shall dwell exhaustively on the Voucher-Based Programmes and collective Investment Programme as viable alternative to Privatizing the public utilities in Nigeria.

Voucher-based programmes involve the distribution of certificates, or coupon, to participants who then exchange their vouchers either for shares in individual public enterprise or for shares in financial intermediaries (voucher funds), which then bid with accumulated vouchers for shares of state owned enterprises. In most cases, vouchers are freely traded for cash. Most voucher-based programme involve multiple financial intermediaries typically unit trusts, although several vouchers programme employ investment trusts for start-up purposes, with the intention of transforming these into unit trusts once the initial stage of implementation is completed. Financial intermediaries offer risk adverse participants investment opportunities in diversified portfolios; they thus serve as clearing houses for vouchers. Voucher programmes have been adopted in the Czech Republic, Mongolia, Poland and Russia with reasonable level of success.

Collective Investment Programme takes the form of investment trusts fund endowed with government-owned equity (Zambia), pension schemes funded from earnings of state-owned enterprises (Bolivia), and in a few instances, non voucher-based unit trust (Malaysia). Collective investment programme differ from voucher-based programmes in two respects.

First, they do not necessarily involve distribution of paper vouchers, and as a consequence, they are more simple to administer and typically require fewer resources for their implementation. Second, participants are usually not allowed to freely enter and exit the schemes. In the case of privatization trust funds, citizens do not individually own shares in the fund or any of the underlying assets; rather, the assets are collectively owned and held for the benefit of current and future citizens. There is no immediate direct financial gain by participants. In the case of pension schemes, participants can only gain access to their share of the fund through retirement or illness. Collective investment programme are more appropriate where there are severe constraints to capital market development, little or no understanding of share ownership, cultural barriers to individual accumulation of wealth, low degrees of literacy, and logistical constraints such as a highly dispersed and difficult to reach population. (See Bell, 1995)

In some cases, collective investment programme, take the form of special unit trusts aimed at increasing the representation of low income groups or ethnic minorities in the economy, as was done in Malaysia. Trustees of these institutions sometimes actively oversee enterprise management and undertake restructuring activities. As noted earlier, all eligible citizens are owners' of the shares, but in name only. There are not immediate tangible benefits to citizens under these arrangements; they receive no share of the proceeds nor dividends. However they may benefit at some future date from discounted public offering of the trust fund portfolio. The attraction of privatization trust funds stems from their usefulness as an institutional vehicle for moving state-owned enterprises out of government ownership and under the supervision of profit-oriented trustees until they can be successfully privatized.

5.0 SUMMARY AND CONCLUDING REMARKS

The paper have examined some issues involved in the economics of public enterprises in Nigeria as well as the theoretical issues in privatization. The paper identified lack of political will as one of the most inept forces that work against privatization in Nigeria. For the attainment of the lofty announced policies of government on privatization, the paper, recommended the adoption of an admixture of voucher based programmes, collective investment programmes and public offering for the country in the next millennium as viable options for privatizing some sectors of the Nigerian economy. If Nigeria is to catch up with the rest of the world in the next millennium, those basic infrastructure including public utilities taken for granted in most other countries must be adequately developed and run efficiently. In our considered opinion, this could only be achieved through a properly sequenced and politically acceptable privatization programme. The time to take action is now, if the future of Nigerians is to safeguard a place in the Committee of civilized nations in the next millennium.

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