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Turning Transitions into Prosperity

Ukraine - Improving the Efficiency and Management of State Enterprises

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Although the privatization of the state-owned sector is expected to increase the efficiency and competitiveness of the country's economy, some of the empirical results suggest that success of privatization programs is mixed (Blanchard and Aghion, 1996; Blanchard and Schleifer, 2000).

Reasons for Mixture Results

- Interests of governments might be different from increasing productive efficiency (i.e., social goals)
- Influenced by their private incentives and lobbies, governments may choose privatization when this is not efficient
- Privatization of some companies and businesses can lead to strengthening of those interest groups, which opposed to further reforms

Some Facts on Ukraine

- Between 1997 and 2004 the number of state owned enterprises (SOE) in Ukraine decreased from **52,836** to **42,935** (annual average decrease of around **2%**)
- Total number of registered in Ukraine enterprises increased from **615,686** in 1997 to **981,054** in 2004 (average by 8% per annum)
- The weight of SOE in the total number of registered in the country enterprises decreased from **8%** in 1997 to **4.3%** in 2004

External Business Environment is a Major Efficiency Factor for Economic Development

- **Competition** - removal of barriers to entry, the elimination of price controls, liberalization of foreign trade, the abolition of preferential regulations, and the break down of monopolistic structures.
- **Hard Budgets.** The government should eliminate any monetary subsidies, and privileges.
- **Market-Based Controls and Discipline** –market is the main regulator
- **Restructuring.** Only the public goods component of the enterprise should remain in the company

Internal Factors of Corporate Governance

- **Corporatization**
- **Agent Representing the State**
- **Role of Board of Directors**
- **Management Arrangements**

Corporatization

Goal: The state enterprise should have a legal status under which there is clear separation between the roles of Owner (the state) and the Manager

How to do: The new draft Law on Joint Stock Companies should be approved

Agent Representing the State

Goal: Dismissed some of the responsibilities of the line ministries to manage SOE. The existing management is inefficient--- (i) it involves conflicts of interest, (ii) possibilities of patronage, and (iii) corruption

How to do: Special amendment on functions of the line ministries

Role of Board of Directors

Goal: Should serve as intermediary between the state and the enterprise managers

How to do: (i) spell out clearly the objectives, responsibilities and authority of the Board; (ii) government officials should be barred from serving in the Boards, to avoid political interferences in management

Management Arrangements

Goal: generate a combination of “returns and risks” similar to those ones confronted by private enterprise managers.

How to do: Different management arrangements are possible: (i) performance contracts, (ii) management contracts; (iii) leasing; and (iv) concessions.

International experience

Common feature of successful management of SOE is a clear distinction between the rights and the responsibilities of the government on state enterprises.

Actual management of the SOE should be done by fairly autonomous entities working under clear performance targets

New Zealand

- state enterprises are run as autonomous commercial entities with independent boards of directors
- shares of each state enterprise are divided between the Ministry of Finance and different sector ministries
- SOE directors are legally bound to act only in the SOE's best interest
- Crown Companies Monitoring Advisory Unit supports two shareholding ministries in overseeing each of New Zealand's 16 SOEs

Norway

- Norwegian government owns and regulates only a few SOEs, of which the biggest is Statoil
- the state has no power over Statoil other than the shareholder rights it exercises at annual general meetings
- the compensation of the management is based on the company's performance

Sweden

- 59 SOEs registered in Sweden produce about 7% of the Swedish GDP and secure 5% of the country's total employment
- The Swedish Ministry of Industry, Employment, and Communications administers the country's SOE
- Ministry has a special division with a staff of 13 people

Poland

- Poland's 512 SOEs were assigned to 15 national investment funds (NIF) for management supervision and control
- each NIF was outsourced to professional asset managers based on the results of a public tender
- each NIF became the lead shareholder in SOEs by receiving 60% of shares, while the remaining shares were distributed among the state treasury (25%), and enterprise employees (15%).

Singapore

- SOEs in Singapore are fully incorporated and controlled by a holding company Temasek, which produces 12% of Singapore's GDP
- The Temasek is fully owned by the Ministry of Finance
- ministry appoints the chairman and members of Temasek's board
- Every year, Temasek submits audited financial statements to the ministry for review