

# **Economic Governance and Development in Vietnam and Mozambique ("FFU Project")**

## **Activity 7: Enterprise Development and Private Sector**

### **A Review of Privatization of State-Owned Enterprises in Mozambique Since 1986**

Sandra Bila\*

Ministry of Planning and Development  
National Directorate of Studies and Policy Analysis (DNEAP)  
Maputo, Mozambique

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\*Sandra Bila ([sandrabila@gmail.com](mailto:sandrabila@gmail.com)): DNEAP, Ministry of Planning and Development (MPD), Mozambique. Address for correspondence: Ahmed Sékou Touré Avenue 21, Maputo, Mozambique, Phone: (+258) 21 49 00 06. We are thankful for productive and stimulating collaboration with the analytical team from University of Copenhagen.

The intent of the FFU working paper is to stimulate and exchange ideas on issues pertinent to the economic and social development of Mozambique and Vietnam. A multiplicity of views exists on how to best foment economic and social development. The discussion paper series aims to reflect this adversity.

**As a result, the ideas presented in the discussion paper are those of the authors. The content of the paper do not necessarily reflect the views of the Ministry of Planning and Development or any other institution within the Government of Mozambique.**

## **Abstract**

Privatization became a central element of economic reform in many developing countries. In Mozambique, a low-income economy privatization of State-Owned Enterprises constituted the core of the country's economic transformation and transition from a centrally planned to a market oriented economy. This study reviews the privatization process of State-Owned Enterprises (SOEs) and its reforms in Mozambique since 1986, and derives some general results, trends and conclusions from the empirical evidence available.

The main findings on the study show that privatization process in Mozambique was similar to the rest of Sub-Saharan African economies. Smaller enterprises were privatized first, while the privatization of large enterprises paced only after donor intervention. By the end of 1990s about 1400 SOEs were restructured, but very limited revenue was collected from privatization proceeds.

The privatization process produced ambiguous results in terms of economic impact. While large enterprises mostly purchased by foreign multinationals have performed well, smaller enterprises have encountered a series of difficulties owing to their weak capitalization, inexperienced management and poor access to credit. Through privatization, the Mozambican economy achieved an expanded and more dynamic private sector, more efficient and effective infrastructure provision and increased investment. . Following these analyses, economic policy to improve the implementation of economic policies and strategies, to improve efficiency of private sector are proposed.

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## List of Acronyms and Abbreviations

|          |  |
|----------|--|
| BM       | Bank of Mozambique   |
| CEMPRE   | Enterprise Census  |
| CEP      | Privatization Execution Commission                               |
| CIRE     | Inter-ministerial Commission for Restructuring                   |
| CNAA     | National Commission of Assessment and Disposal                   |
| CPAA     | Provincial Commission of Assessment and Disposal                 |
| CPI      | Center for Investments Promotion                                 |
| CTA      | Confederation of Business Association                            |
| DNEAP    | National Directorate of Studies and Policy Analysis              |
| DPR      | Diagnosis for Potential Restructuring                            |
| DUAT     | Direito de Uso e Aproveitamento de Terra                         |
| GDP      | Gross Domestic Product   |
| GoM      | Government of Mozambique   |
| GREAP    | Office of Corporate Restructuring Agricultural and Fishery       |
| GREICT   | Office of Corporate Restructuring of Industry, Trade and Tourism |
| ICA      | Investments Climate Assessment                                   |
| IMF      | International Monetary Fund                                      |
| INE      | National Institute of Statistics                                 |
| MAP      | Ministry of Agriculture and Fisheries                            |
| MICTUR   | Ministry of Industry, Commerce and Tourism                       |
| MINEC    | Ministry of Education  |
| MPF      | Ministry of Planning and Finance                                 |
| PARPA II | Action Plan for the Reduction of Absolute Poverty (2005-2009)    |
| PRE      | Program of Economic Restructuring                                |
| PRES     | Program of Social and Economic Rehabilitation                    |
| RPED     | Regional Program on Enterprise Development                       |
| SMEs     | Small and Medium Enterprises                                     |
| SOEs     | State-Owned Enterprises  |
| SSA      | Sub-Saharan Africa   |
| UTRE     | Technical Unit for Restructuring of Enterprise                   |
| WB       | World Bank   |

## 1. Introduction

The economy of Mozambique has been registering a satisfactory economic progress and development since the end of civil war (1977-1992). The Government of Mozambique (GoM) has been promoting the implementation of diverse and strong macroeconomic policies to achieve an accelerated economic growth, sustainable development and reduce poverty as desired.

Mozambique has recorded an average Gross Domestic Product (GDP) growth rate of 7.44 percent in the past 15 years.<sup>2</sup> This economic growth was accompanied by a reduction in the poverty rate in the country, approximately 69.4 percent in 1997 to 54.1 percent in 2004 poverty evaluation. This improvement is a reflection of the country's efforts to enhance macroeconomic and fiscal management, and structural reforms aimed at uplifting the economic situation of the country.

In developing countries privatization constituted the center of structural and economic transformation. The motives for privatization have encompassed improved fiscal equity and distributional performance, although the importance attached to each has varied between and within countries over time. By the end of 1980s privatization became a central element of economic reform in many developing countries. Mozambique was no exception; where the privatization of SOEs constitutes the core of the country's economic transformation and transition from a centrally planned to a market oriented economy, contributing significantly to the present economic progress.

On the ambit of the economic governance and development between Vietnam and Mozambique (FFU project) this study aims at analyzing the economic reforms and privatization process of State-Owned Enterprises (SOEs) in Mozambique since 1986. This information is essential for understanding the present structure of the private sector and effectively formulates future policies aimed at the private sector. This study's challenge is to answer three main question: i) which concrete measures/policy have been used to achieve greater economic efficiency, ii) how has the process of privatization of SOEs been undertaken, and iii) what can be said about the socio-economic impact of the privatization process.

The organization of the paper is as follows: in section 2 it's attempted to underscore the economic and political basis of state-owned enterprises in the Mozambican economic context. Section 3 gives an overview of economic reforms implemented towards privatization, with attention to the legal framework of the privatization process. The structure and procedure of privatization is presented in Section 4, while section 5 presents and discusses the results of the evaluation of impact of privatization process. Finally, section 6 concludes and presents some policy recommendations.

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<sup>2</sup> MPD/DNEAP Macroeconomic framework 2010.

## 2. Theoretical Background

Across the globe, privatization has grown in popularity and acceptability. It has also become an important instrument used by governments to promote economic development, improve economic efficiency and stream line government structure. Privatization has become an acceptable paradigm in political economy of States. It is a strategy widely used for reducing the size of government and transferring assets and service functions from public to private ownership and control.

Economics schools have tried to explain the variation of policies applicable to privatization. The main schools of thought Laissez-Faire classical economy, public choice approach, populist approach and the pragmatist school, advocate alternative approaches to enable the government to provide services with the highest possible efficiency. According to these schools of thought, privatization would reap the advantages of effectiveness, productivity and efficient production and delivery of goods and services. In addition, privatizations will also strength market forces with some degree of deregulation, economic liberalization, relaxation of wage and price control (Adayemo and Adeleke, 2008).

Privatization has become an acceptable paradigm for political economy of states. In developing countries, it was widely used to improve productivity and efficiency of state-owned enterprises, access investment capital and improve service delivery of high cost critical sectors that impact the economy as a whole; and reduce the fiscal burden of loss-making firms.

During the 1990s there was a boom in privatization activities. The overall trend in developing countries shows a drop in privatization activity after 1997, but picket up albeit modestly. During 2000-2003, about 120 developing countries carried out a total of 7860 transactions, generating a total of about \$410 billion in privatization proceeds. The Middle East and North America region raised a total of \$19 billion (5 percent) of total proceeds from 310 transactions, while the South Asia raised a total of \$15 billion (4 percent) from nearly 400 transactions. Sub-Saharan Africa (SSA) had the 3<sup>rd</sup> highest number of transactions but only raised \$11 billion proceeds representing just 3 percent of total proceeds from 960 transactions (Kikeri and Kelo, 2005).

Analysis of sector trends for developing countries show that infrastructure, competitive and financial sectors accounted for about 84 percent of privatization proceeds. Infrastructures (i.e.: telecommunication, electricity, transport and water) accounted for half of privatization proceeds, competitive sector (i.e.: manufacturing, services and tourism) accounted for 19 percent and energy 15 percent of total proceeds (Kikeri *et al*, 2005).

The privatization of SOEs enterprises would tend to suggest that government ownership has declined over the years. But a systematic assessment is difficult in the absence of data on state enterprise sectors, in particular their share of GDP, investment, domestic credit, formal sector employment, and the like. Nevertheless, in SSA government ownership is widespread. While state enterprises in 1991 accounted for 17.3 percent of GDP in African countries (World Bank

1995), total privatization proceeds since 1990 amounted to only 0.2 percent of regional GDP. Another estimate suggests that state enterprises in SSA still account for over 15 percent of GDP on average (Chong and Lopez-de-Silanes, 2004). In competitive sectors, over 300 enterprises in over 30 countries that have long been earmarked for privatization are still pending for sale (OECD, 2004).

Government ownership in existing infrastructure continues to exist despite increasing emphasis on private sector participation over the past decade. In SSA, a substantial large proportion of power utilities, telecommunication and transport and water utilities are still owned and operated by the State (World Bank, 2007). On the other, the government participation in the financial sector has reduced significantly.

Most of privatization programs implemented thus far have been proven to be economically successful. In the vast majority of cases the results from privatization improved enterprise performance and increased state revenue. Most privatization success stories come from high-income and middle-income countries. Nonetheless, successes can be found in low-income countries, too. Privatization turned around an almost moribund textile firm in Niger, helped revive a defunct development finance corporation in Swaziland, and revitalized an agro-industrial firm in Mozambique. The Mozambican firm diversified into new products, began servicing its debts, and increased production fivefold (World Bank, 1992; Megginson, 1998; Young, 1998).

The experience from the past several years shows that privatization is neither a panacea nor a universal solution that can be easily applied to all countries and sectors. There is no privatization approach, procedure or modality that suits every country. Instead, policies and approaches need to be formulated by taking into account sectoral and country circumstances, in particular market structures and levels of institutional and economic development.

The distributional impact of privatization in SSA has been overlooked by a large extent. Consequently, very little is known about its social impact. Additionally, privatization is essential in creating a competitive framework. However, it is a necessary but not sufficient condition for economic efficiency of the economic sectors which privatized firms operate. Therefore, business environment

### 3. Privatization in the Mozambique Context

Privatization can be defined in several ways, depending on the form it takes. Privatization can be defined in several ways depending on the form it takes. Privatization in Mozambique is referred to a transaction in which ownership or control of a public body (state, government, ministry, department, enterprise or corporation) or its major assets or shares held by a public body in a company representing a controlling interest are to be transferred from the government or a government-controlled entity to the private sector (World Bank). This section places privatization in the Mozambican context, looking at the basis towards the privatization of SOEs.

#### 3.1. The Establishment of State-Owned Enterprises

The economic transformation of many developing economies has been dramatic. In Mozambique, the decolonization process marked the beginning of the political transition period around 1974/1975. During this period, many enterprises and businesses were abandoned by the Portuguese owners and managers that fled the country, leaving them to the employees who (in many instances) had very little knowledge and experience about enterprise management.

After the proclamation of independence in 1974, the Government of Mozambique (GoM) increased its intervention in economic activity. Its involvement in business activities and enterprises that for various reasons did not contribute to economic growth and development was noteworthy. During this time, the GoM began to introduce a series of reforms aimed to regulate, control and increase efficiency of production of vital enterprises.

The 3<sup>rd</sup> congress of FRELIMO<sup>3</sup> attributed the state the main task, to organize the productive sector as a way to secure the centralized direction of the economy, promote its planned management, develop and consolidate the state's sector of production which must be a fundamental economic domain (Saturnino, 2008:273-274). The approval of Decree 16/75, proclaimed a number of strategic measures to regulate entrepreneurial economic activity in strategic sectors. The underlying philosophy that monopoly in some sectors, should belong to the government to ensure the production and distribution of goods formed the basis for this policy. According to *Tribunal de Contas*<sup>4</sup> (2002) choosing economic sectors by its economic or social importance was to ensure standard quality and systematic training of technical staff.

The concept of State-Owned Enterprises was born and won legislative consecration after the approval of a legislative pack during 1975-1979.<sup>5</sup> The use of the approved decree and laws

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<sup>3</sup> FRELIMO stands for *Frente de Libertação de Moçambique*.

<sup>4</sup> In English - Court of Auditors.

<sup>5</sup> The formalization and development of state-owned enterprises was achieved by the approval of Decree-Law 17/77 and 18/78 both dated 28<sup>th</sup> April.

became widespread, and the intervention of stock companies and other enterprises created by the state, would be regarded as state enterprises under the government's economic policy.

The law of organization and functioning of SOEs Law 3/81, defines the principles governing the operation of public enterprises.<sup>6</sup> State enterprises were owned by the state with the following features: i) legal personality, ii) administrative, financial and property autonomy, iii) exempted from income taxes (but required to deliver to the treasury a percentage of their net income), and iv) accounts were not subject to review by administrative court.

The SOEs constitute an important element in the construction of the material, political and ideological base for the edification of the new society and for the planned economic development. As the main catalyst of development of national economy must assume the priority responsibility of resizing the objectives defined by the state.

### **3.2. Classification of State-Owned Enterprises**

State-Owned enterprises in Mozambique are classified in three categories, namely: public enterprises, publicly owned enterprises and state shareholding enterprises. Public enterprises are collective persons with their own legal status and autonomy over administrative, financial, and asset management issues, in which the State holds 100 percent of the capital stock. These enterprises only operate in public utility sectors such as Electricity (i.e.: Electricity of Mozambique - EDM), Water and postal services (i.e.: Correios de Moçambique).

The publicly-owned enterprises are those in which the State, sometimes in conjunction with a public enterprise, is the sole or major owner of the capital. These enterprises are present in telecommunications (i.e.: Telecommunication of Mozambique - TDM), air transport (i.e.: Mozambican Airlines - LAM), imports of medicines (i.e.: MEDIMOC) and recently also in the oil and gas sectors (i.e.: Petroleum of Mozambique).

And lastly, State Shareholding enterprises are those enterprises in which the State holds a major shareholding in private enterprises, sometimes as a result of reverting to the State ownership enterprises that were involved in unsuccessful privatization process, or as a result of the State's intention of having a presence in strategic sectors. Currently the state has holdings in about 134 enterprises in Mozambique, this include Mozal (i.e.: Aluminium Smelter) and Moçambique Celulares (i.e.: Cellular Service Provider company MCell).

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<sup>6</sup> This law was then substituted by the Law 15/91, the law of State-Owned Enterprises.

### 3.3. Legal and Institutional Framework of State-Owned Enterprises

The operation and management of public enterprises is governed by the Law of Public Enterprises.<sup>7</sup> The law of public enterprises sets out the rules for the creation, organization, and operation of state-owned public enterprises and their relations with central government. Only the first type of SOEs, presented in the above section is regulated by this law, the other two operate in compliance with the commercial code.<sup>8</sup>

In principle, the law of public enterprises stipulates that SOEs are subject to: i) the same tax and labour regimes as private sector, ii) contract loans subject to authorization by the Ministry of Finance (MF), iii) entitled to compensation via a transfer from the state budget should they be required to execute a public pricing policy, and iv) can benefit from outstanding special loan agreements.

The legal framework governing the operation of public enterprises is ambiguous. Despite the rules specified by the law of public enterprises, it has loopholes on the following aspects: i) it is not clear what is the rights of the MF to conduct financial oversight of public enterprises, ii) MF lacks effective legal tools to exert its authority over public enterprise in certain domains, such as distribution of dividends, signature of program-contracts, and collection of the principal and interest payments on special loans, iii) it is not clear either whether the legal framework governing public enterprises extends to any such enterprises that local governments may create, iv) the legal and management framework governing publicly-owned corporations is unclear, since such corporations are not covered by the Public Enterprise Law (IMF, 2008). This reflects the urgent need for strengthening the legal framework for public enterprises and state autonomous institutions.

In terms of institutional framework, state holdings are managed by the Institute of Management of State Holdings (IGEPE) and National Treasury (Ministry of Finance). The IGEPE was created in 2006 and attributed the responsibility to coordinate the management of state holdings. The main objective of this institution is to enforce the intervention capacity in the management of state enterprises, aiming to capture incomes resulting from dividends of participating societies. Currently, the portfolio of state holdings managed by IGEPE is composed by 134 enterprises.

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<sup>7</sup> Law No. 17/1991 of 3<sup>rd</sup> of August which establishes the rules for the management of enterprises with state's capital.

<sup>8</sup> The commercial code was approved by Decree-law No.2/2005 of 27<sup>th</sup> December. It provides a regulatory framework for creation and operation of private enterprises as well as commercial societies. Publicly-owned enterprises and state-shareholding enterprises are governed by this law.

## 4. Economic Reforms Towards Privatization

In Mozambique, the privatization of SOEs constitutes the core of economic transition, from a centrally planned to a market oriented economy. Privatizations are part of the process of economic reforms and restructuring that started around the mid-1970s. Subsequently to the failing attempt to control the economy at central level, at the end of 1980s the GoM adopted a series of structural readjustment measures aimed at gradually reducing the role of the state in the economy. The government allowed the intervention of other economic agents, in order to give greater dynamism and more efficient economic activity.

This section analysis the reforms and privatization process towards economic restructuring in Mozambican economy. The objectives of this section are the following: i) describe the legal and institutional framework for privatization process, and ii) analyze the organizational structure of privatization.

### 4.1. Legal and Institutional Framework of Privatization

In Mozambique the economic restructuring process was initiated by the Program of Economic Restructuring (PRE).<sup>9</sup> The PRE was initiated in 1987 and has led to the liberalisation of the economy and also paved the way for greater involvement of the private in the economy on behalf of the state. During the early years of the PRE, was enacted several legislation which established the mechanisms for the privatization, divestiture and sale of state's holdings. In other words, the PRE defined the legal basis that characterized the methods which the restructuring of SOEs has to be developed and processed. **Error! Reference source not found.** Presents a summary of the rivatization legislation.

Table 1 presents the laws that provide the general rules applicable to the total or partial privatization of enterprises of which the State and legal entities governed by public law own, directly or indirectly, all or part of the capital.

The privatization exercise in Mozambique was defined under the Decree 21/89. This decree regulates the sales of state-owned assets through a public tender and establishes the administrative procedure for sales. As a complementary, law 15/91 was enacted. It established the norms for the restructuring, transformation and reshaping of the state's enterprise sector, including the privatization and alienation of enterprises, establishments, installations and state's holdings.

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<sup>9</sup> The Economic Rehabilitation Program (PRE) is further discussed in section 4.2.

**TABLE 1: LEGAL BASIS FOR PRIVATIZATION IN MOZAMBIQUE**

| <b>1986-1989</b>   | <b>1990s</b>  | <b>2000-currently</b>   |
|--|---|---|
| Law that allows the sale of state holdings.  | Law that states which enterprises intervened by the state may become SOEs.                          | Decree-law that establishes the strategy for the restructuring of enterprises with state participation.     |
| Law that establishing the framework for investments.   | Law that establishes the norms about the restructuring and re-dimensioning of SOEs.                 | Commercial code that stipulates the regulatory framework for creation and operation of private enterprises. |
| A law that puts in place dispositions that allow increased competitiveness and functioning to the state's business sector. | Law that defines the judicial framework and administrative process for restructuring.               | Legislation that regulates the licensing of industrial and commercial activity.                             |
|  | Law that creates the inter-ministerial commission for Restructuring of SOEs (CIRE).                 |   |
|  | Law that attributes UTRE the function to coordinate the privatization process of large enterprises. |   |
|  | Law of public enterprises that regulates the operation of SOEs.                                     |   |
| Source: UTRE, Ministry of Finance (1995) and Saturnino (2008:303).   |   |   |

Under decree 30/91, 3/93 and 4/94 identify the SOEs to be privatized. In addition, Decree 20/93, establishes the procedures to follow regarding the acquisition of shares by managers, technicians and workers. It was also published Law No. 17/92 of 14 October, by fixing an interpretative common understanding that seeks to ensure proper implementation of art.16 of Law 15/91, concerning the acquisition of shares by managers, technicians and workers.

During the restructuring phase, specific bodies to undertake the privatization process were created. The Decree 27/91 created an Inter-Ministerial Commission for Enterprise Restructuring (CIRE), an advisory body to the Prime Minister in the process of enterprises the restructuring.

Furthermore, the Ministerial Diploma 87/92 creates the Technical Unit for Enterprise Restructuring (UTRE) within the Ministry of Planning, and attributes the main task of coordinating the entire process for the restructuring of large enterprises. In the case of Small and Medium Enterprises (SMEs), the privatization process is undertaken by UTRE and the relevant ministries.

One of the objectives of the restructuring of the business sector is the growing involvement of Mozambican investors in the process of transferring state enterprises to the private sector. Thus, the Council of Minister approved a law to facilitate access to Mozambican investors in the process of restructuring.<sup>10</sup> The law encourages national entrepreneurs by extending the terms of payment, application to a favourable interest rate and the possibility to the contractor to mortgage the acquired good (as collateral) up to 60 percent of its value even before full payment.

The economic restructuring program revealed that the legal regime applicable to state-owned enterprises was greatly exceeded. Thus, a new public enterprises law was established. Law 17/91 establishes the rules for the organization and functioning of public enterprises. This law was promulgated as new legal mechanisms to ensure a more efficiency and profitability of the state's business sector. It was complemented by the commercial code and legislation that regulates the licensing of industrial and commercial activity.

## **4.2. Structure of Privatization Process**

Under the Economic Rehabilitation Program, the government established a program for restructuring, transforming and resizing the state enterprise sector.<sup>11</sup> This stage of state economic policy, allowed the possible reverse of the economic crisis that characterized the early years of independence. However, several state agencies and other productive units lacking legal personality (not exactly SOEs) connected to state-funded projects and/or international bodies never came to regularize their legal situation. As a result, reducing the capability of its relation with other enterprises and leading to a period of weak business performance.

The economic growth and development achieved in the country during this period, was further adversely affected by the effects of the civil war that rocked the country and the economy in 80 years. After the civil war, most of the SOEs were characterized by serious structural problems, such as: i) obsolescence of equipment and technology, ii) management problems, iii) severe market problems and low capacity utilization, iv) excessive labour and wage arrears, v) high level of debt to banks and subsidies from state, and vi) shortage of financial resources to conduct

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<sup>10</sup>On the 6th May 1997 the Council of Ministers approved the Decree 10/97 which amends the Decree 21/89 of 23 May that introduces changes to Decree 21/89 of 23<sup>rd</sup> May, facilitating the access of the Mozambican investors in the enterprise restructuring process.

<sup>11</sup>This program was defined by the Law 15/91 of 3<sup>rd</sup> of August.

the maintenance and rehab. Consequently, the government come to a decision to privatize most of the enterprises with weak performance, as a means to boost economic growth and development.

The concept of privatization in the Mozambican context refers to transfer of the ownership of economic entities from the state to private agents, jointly with the transfer of decision-making on economic parameters (i.e.: prices) from state to the market forces.<sup>12</sup> The privatization process was undertaken in two distinct phases, namely: i) Deregulation in the period of 1986-1989) and ii) Denationalization in the 1990s, discussed in the sections that follow.

#### *4.2.1. Deregulation (1986-1989)*

After the failed attempt at central planning and the civil war paralyzed Mozambique's economy, the government undertook the dual tasks of reaching a peace settlement and effecting the transition from centrally planned to a market-oriented economy. The government started a series of economic reform aimed at reorganizing the state's business sector and privatization, initiated by the Program of Economic Restructuring (PRE) introduced in late 1980s.<sup>13</sup>

The process of enterprises restructuring assumes a fundamental importance in the Program of Economic Restructuring (PRE). The stabilization and structural reform program sought to address the fundamental causes of Mozambique's economic crisis (World Bank, 2001). The donor community strongly supported the PRE. The implementation of this program markedly increased the assistance of donor community to Mozambique. The World Bank and IMF were been strongly involved in the formulation of the PRE and especially in the privatization of large enterprises.

The PRE marked the beginning of the deregulation phase. The PRE was initiated in 1987 and it set out the basic conditions for the sale and privatization of SOEs to take place. The PRE led to the liberalisation of processes, a continuous devaluation of domestic currency and cuts in the government expenditure. As a consequence, the economy registered a severe drop in the purchasing power of Mozambicans, and the terms of trade worsened, especially for producers selling to the local market (Trop and Rekve, 1998).<sup>14</sup>

Outside the privatization program, the government undertook the deregulation and concession of activities of SOEs. This process included the ongoing concession of railways, port and port services owned by national ports and railways company (CFM) and the concession of water

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<sup>12</sup> The privatization process in Mozambique was characterized by both deregulation and denationalization.

<sup>13</sup> The legislation for the economic and social rehabilitation program was started by Decree No. 21/89 of 23<sup>rd</sup> May.

<sup>14</sup> The recovery program and liberalization of the economy has had its prime impact on the terms of trade within the sector, with a notable decline between the sale of fish and the buying of equipment needed for fishing constituting one of the main constraints (Trop and Rekve, 1998).

delivery in five major cities (i.e.: Beira, Maputo, Nampula, Pemba and Quelimane). Deregulation was the appropriate first step towards improving service quality and plugging the unsustainable drain on public finances. In other words, deregulation was chosen as a short-term substitute for privatization, based on the urgent need to reduce pressure on the budget from financially insolvent SOEs.

Under the PRE, the government paved the way for greater involvement in private sector in the economy on behalf of the state. The legislation for the PRE approved the laws regulating the privatization through sale, divestiture or joint venture of state-owned enterprises, establishments, facilities and other forms of financial participation by the state.

With substantial external financial and technical assistance, the PRE began rehabilitation the country's infrastructure and human resource base, while simultaneously stabilizing the jump-starting the economy. Consequently, diminishing public expenditure on non-profitable economic activities and increased production through the activities of more efficient economic agents.

This action was continued and supplemented by the publication of a law implemented within the strategy for downsizing and streamlining the business sector. The law No. 15/91 of 3<sup>rd</sup> of August establishes the norms for the restructuring, transformation and re-dimensioning of the State's business sector.<sup>15</sup> It legally defines the way for the settlement of controversial situations and for restructuring, integration or dissolution of companies regularly given as intervention stock.

The process of privatization in Mozambique, besides the actual privatizations of state business enterprises, it also encompassed a set of measures to encourage private investment as a way to strengthen the private sector. Additional reforms were introduced to start restructuring the economy, such as Decree-Law No 5/87 of 19<sup>th</sup> January and Decree No 10/87 of 30<sup>th</sup> January established the frame of investments incentives for national and foreign investors.

Later in 1990s, further legislation to harmonize and accelerate the privatization process was introduced. The liberalization of the economy and increased private sector participation in the production process are basic deregulation measures that constitute the overall framework for the denationalization of SOEs.

#### 4.2.2. *Denationalization (1990s)*

The second phase of privatization initiated with the implementation of a new legislative pack at the end of 1989. It was characterized by denationalization, that is, the transfer of ownership of

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<sup>15</sup>States business sector is the group of public and state-owned enterprises, commercial societies (partnerships) in which the capital belongs exclusively to the state, and/or other collective persons of public rights, enterprises, establishments and installations whose ownership was reverted to the state (Saturnino, 2008:286).

economic entities from state to private agents. It constituted the basis of the privatization in Mozambique.

In early 1990, the Mozambican economy registered a boom in the privatization of SOEs. During this period, complementary privatization policies were set up under the influence of international donor community. The World Bank and IMF increasingly stressed the need for fast privatization and advocated private ownership as an instrument for economic efficiency and development. Consequently, new agreements with the World Bank and IMF were signed to ensure that privatization remained a priority in Government agenda.<sup>16</sup> There were two main arguments in support of privatization of Mozambican SOEs: Firstly, SOEs inefficiency lead to deterioration of the economy and a fall in the manufacturing output over 1990-1994, and secondly, a reduction of fiscal burden of SOEs losses would free public revenue for use elsewhere (Castel-Branco *et al.*, 2001). Consequently, the priority of privatization in the government policies constituted a prime condition for continuous financial help from donors.

However, it was not until 1991 that the objectives of privatization were defined. The main goal of privatization was to gradually reduce the role of the state enterprise and provide the intervention of other economic agents in order to give greater dynamism, stimulate economic activity and increasing efficiency and competitiveness of enterprises. The enterprise restructuring program also aimed at the following:

- Generate income to the state
- Promote the development of the capital market
- Promote the dissemination of social capital through the access to ownership of shares in companies by citizens in general and workers in particular
- Reduce the involvement of the state on the process of business decision
- Attract private domestic and foreign investment, allowing to recapitalize the companies, rehabilitating them or expanding their production capacity
- Promote technological and organizational changes in order to increase efficiency and competitiveness
- Modern management techniques, develop the productivity of work and encourage raising the skills of technicians and workers
- Raise the quality of products and services and increase and diversify its offer to contribute to the improvement of supply and functioning of markets and increase exports
- Promote a dynamic economic activity, through the intervention of the private sector
- Reduce the weight on government budget resulting from the subsidies directly/indirectly attributed to the SOEs, and
- Reduce the government involvement in the business decision-making process

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<sup>16</sup> In 1989, the World Bank approved two credits to support the privatization process, the Small and Medium Enterprises Project (SMEP) and Industrial Enterprise Restructuring Project (IERP) to boost the industrial production.

The Mozambican legislation allowed for the participation of foreigners in the process of privatization. The participation of foreigners was prioritized only when additional investment was needed in high technology was not available domestically, and where access to new markets and increase in exports implied the use of mechanisms for converting the country's foreign debt. Moreover, for the establishment of new enterprises, there were no limitations in the participation of foreign investors.

In terms of privatization methodologies, the restructuring of the state enterprise sector could take different forms, all of which entail some form of private sector participation in product or service delivery. The most common forms of privatization of SOEs used in Mozambique are:<sup>17</sup>

- a) Asset of Sale – consists in the selling off the asset of an enterprise, probably following a cessation of operations. When it was expected influx of candidates was considerable large, the sale was performed by means of public tender. In case of equal scores preferences were given to Mozambican nationality and the fighters of the National Liberation Struggle.
- b) Sale of shares - it provides the public the opportunity to purchase shares in a society with limited liability. The sale may be made based on the best offer or price fixing, fixing also limit the shares that a single investor can acquire.
- c) Private negotiation or tender, preceded by the prospect of partners and pre-qualification, respectively - negotiating is done separately, after prospecting of potential stakeholders. Proposals received are evaluated based on the review of development plans and rescue the company, the technical capacity demonstrated by vocation and experience of the bidder and guarantees as to the suitability commercial, financial, industrial and fiscal. In addition, it is also taken into account the price and payment terms.
- d) Private investments, including the issuing of new shares in SOEs – it used whenever there is need to raise capital to allow for new investment in the rehabilitation or expansion of productive capacity/service in order to improve the management, technological modernization, diversification productions or activities and access to markets.
- e) Divestiture or Sale of Shares to managers and employees – a portion of shares on offer are reserved for the employees in the SOE. The sale of shares is only applicable for employees working fulltime for at least five years and paid by the enterprise. Pensioners and retirees of the company or establishment subject to alienation can also

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<sup>17</sup> This was defined by Decree No 28/91 of 21<sup>st</sup> November. The privatization procedures could be applied separately or in combination.

acquire some shares. Furthermore, individual buyers could acquire share equivalent to maximum limit of 25 percent of the capital reserved for them or 10 percent of company's capital.

- f) Management Contract – the responsibility for the provision of services that were hitherto provided by a state-owned firm is passed on to a private provider. Shares acquired in this way are not transferable for a period of 5 years, within which they will be registered, except, of course, situations involving legal succession transmissibility. For managers, technicians and workers of the company these shares are transferable within 3 years.

## 5. The Privatization Phases and Process in Mozambique

Majority of the developing countries in Africa have embarked on the process of privatization. At the time when this process boomed, many governments were hesitant about it. Today, the interest is in the progress and outcome of privatization in the countries embarked in it. This section looks at how SOEs were privatized in Mozambique, by describing the privatization phases and process.

### 5.1. Privatization Phases

The privatization process of SOEs is divided into five stages, namely:

- 1) *Analysis and Study of Enterprise Situation* - elaboration of the Diagnoses of the Potential Restructuring (DPR) is the first stage of the preparation process of an enterprise to be privatization. The DPR characterizes the enterprise in terms of its financial, economic, technical and legal situation.<sup>18</sup> The summary and conclusions of the DPR is prepared by UTRE and submitted with the restructuring proposal to CIRE for the approval, as a means to procedure with the privatization. With the approval of the procedure the Prime-Minister nominates CEP.
- 2) *Outreach and Marketing* – once the process of alienation is approved, begins the phase of pre-qualification (For example, in case of restricted tendering), though the publication of announcements and editorial coverage in the local and international press, and direct correspondence with the investors who had manifested interest in the enterprise to be privatized.
- 3) *Tendering* – after the pre-qualification of candidates, the dates for the tendering are announced and investors are contacted. A Memorandum of Sale (MV) featuring the company in detail, and the procedures and schedule of privatization is made available to pre-qualified bidders by purchase. In case of public tender, the MV is sold without pre-qualification of investors. The bid lasts for two to three months.
- 4) *Evaluation of Proposals* – by the deadline of the tender, the CEP opens the tenders received. And then made their assessment according to technical and financial proposals.<sup>19</sup>

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<sup>18</sup>It can be internally prepared by the enterprise or by UTRE by means of an external consultancy service.

<sup>19</sup>The Technical Proposal was evaluated based on new investments and method of financing, technical capacity and management of rivals, experience in the sector, training and transfer of know-how to national employees. And

- 5) *Negotiation and Signing of Contract* - within 30 days following the close of tender, the CEP decides on the winning bidder. The winner is then invited to the negotiation, and for this purpose have to pay a value equal to 5 percent of the reference price, which can be provided through bank guarantees. The negotiation is completed only after both parties sign the deed for the establishment of a new society and a term delivery of the assets of the company.

## **5.2. Process of Privatization**

The privatization process was based on the regulation in place by mid 1990s. The restructuring of SOEs follows different mechanisms and procedures for large, small and medium (SMEs), and banks. The section that follows looks at the distinction in the privatisation process of these three distinct groups of enterprises.

### *5.2.1. Large Enterprises*

The Mozambican privatization process has been similar to the other African economies. Smaller enterprises were privatized first, while the privatization of large enterprises was left to a later stage (Cramer, 2001).

The privatization of large enterprises was initially very slow, but accelerated after 1995. As a consequence, it delayed the enterprise restructuring within the industrial sector with an undesirable impact on output and overall macro-economic stability (World Bank, 1995). Several reasons account for the slow pace of privatization of large firms, including the delays incurred in the preparation of an appropriate institutional and legal framework for privatization, and the political and economic uncertainty generated by the civil war.

Because of the lack of domestic savings, the privatization program in the post-war period depended critically on the country's ability to attract foreign investment either through direct sales or joint ventures.

UTRE was set up to oversee the privatization and restructuring of about 20 large enterprises. With the exception of the national airlines,<sup>20</sup> all of the enterprises in the original privatization list

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financial proposal, the financial and legal guarantees presented, and the price and condition of payment were the main factors taking into account.

<sup>20</sup>Because of the lack of acceptable bids, the Government converted the airline into a limited liability company, with the intention of selling state's shares on the stock exchange.

were either restructured or privatized by early 1999. Majority shares of more than 85 large enterprises in the original list of enterprises to be restructured were privatized. In addition, about 20 enterprises resulted from enterprise consolidation from the central planning era, and 85 enterprises were either restructured or privatized under new privatization program. The state retained shares in almost all the large enterprises that were privatized.

The procedures established by UTRE for the privatization of large firms have been excessively lengthy and complicated. The restructuring of large firms identified by the Decree of the Council of Ministers, or sent directly to UTRE by regulatory, is coordinated by the Technical Unit which assures the participation of the Ministry of Planning and Finance at the Technical Board of CIRE, and the Secretariat of the Committee. The final decision about the alienation of these enterprises, establishments and social participations was the responsibility of the Prime-Minister.

For each of the companies to be privatized is appointed, the Prime Minister, their Executing the Privatization Commission (CEP), which includes a representative of the Ministry, Bank of Mozambique (BM), Ministry of Planning and Finance, Centre for Investments Promotion (CPI) and a union representative.<sup>21</sup> The functions of CEP, included among others, the pre-qualification of candidates, the evaluation of competing proposals and negotiations with the selected candidates. Diagram 1, illustrates systematically the process of privatization for large enterprises.

A number of problems specifically associated with the privatization process itself have been identified. This problems and difficulties needed to be addressed in order to speed up and ensure a successful privatization program. Some of the problems included: (i) lengthy preparatory procedures; (ii) excess labour issues; and (iii) the need for additional transparency in the bidding and sales process.

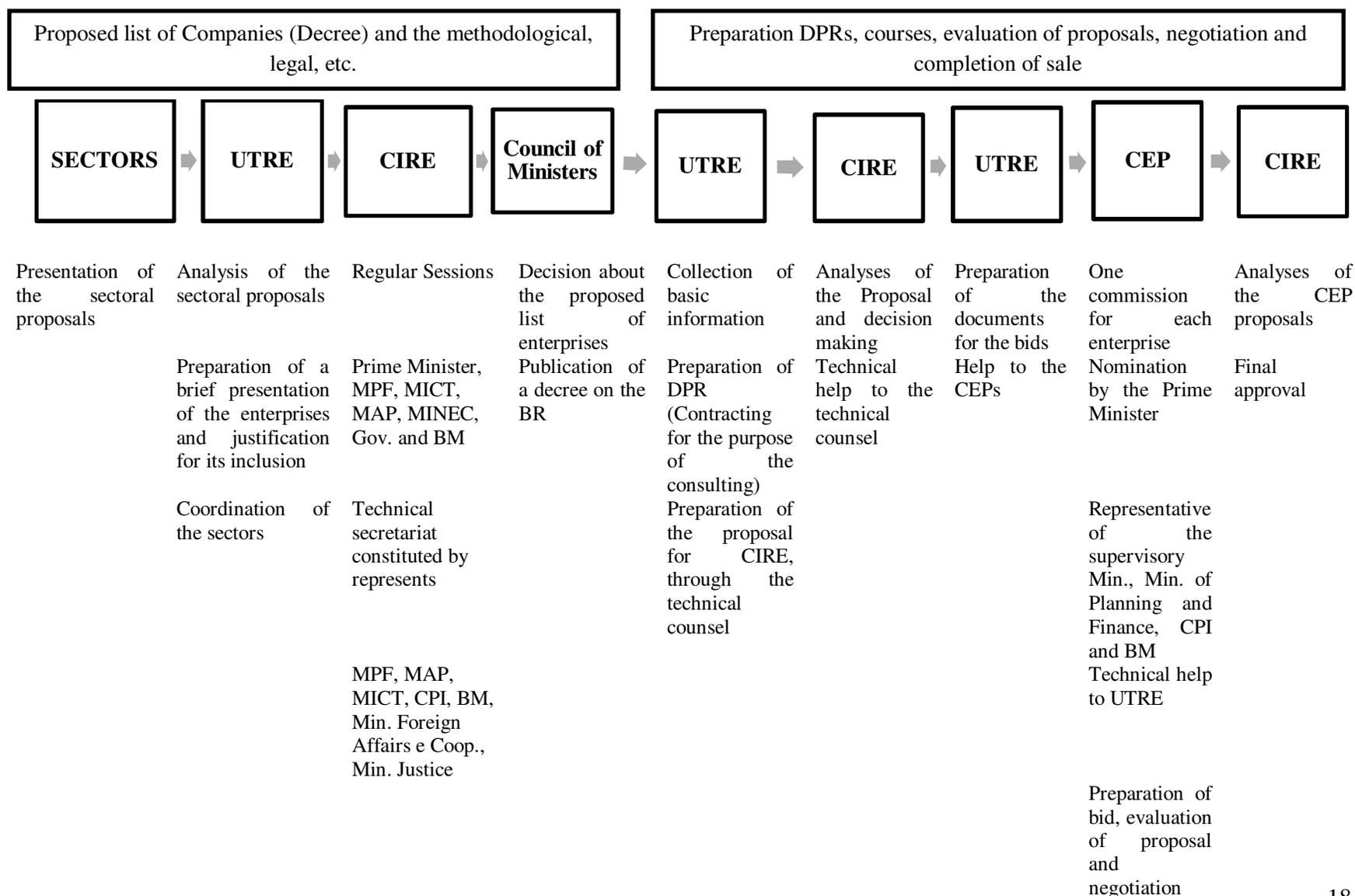
The preparation process of the Diagnoses of the Potential Restructuring (DPR) constituted a major obstacle for privatization of large enterprises. The DPR required large amounts of information and could be expensive (i.e.: \$100.000 - \$300.000 American dollars) and lengthily taking up to one year to complete. Furthermore, the price determination of enterprise to be restructured was ambiguous. The government set a minimum tender minimum price, based on the net present value of the cash flow generated by a proposed investment, reflecting the present value of the enterprise financial and physical assets. The company's 'reference price' was hypothetical and has the potential of discouraging prospective investors unless appropriate clarifications are given. Consequently, enterprises were sold cheaply. Because the minimum tender price were set low in order to encourage bidders, and given the fiscal crisis, the government also needed immediate revenue; future revenue streams were therefore discounted at rates considerably higher than those of the private sector (Castel-Branco *et al*, 2001; Cramer, 1998).

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<sup>21</sup>The CEP is technically and administratively supported by UTRE and the final decision on the sale of these companies, businesses and shares the responsibility of the prime minister.

# THE PROCESS OF PRIVATIZATION FOR LARGE ENTERPRISES

(Art.14 of Law N° 15/91)



### 5.2.2. *Small and Medium Enterprises*

The privatization of Small and Medium (SMEs) was relatively rapid and almost exclusive to Mozambican nationals. Immediately after the decolonization, the political party *Frente de Libertação de Moçambique* (FRELIMO) took power and annexed most of the small business and shops owned by the fleeing Portuguese settlers (Cramer *et al.*, 2002). During the privatization period, many of these enterprises have been sold cheaply to nationals as part of the country's affirmative action (Mugerwa, 2002).

The privatization procedure for SMEs follows a sectoral/provincial methodology. Once the enterprises are selected by the various line ministries, these enterprises have the National Commission of Assessment and Disposal (CNAA) in each sector or the Provincial Commission of Assessment and Disposal (CPAA) responsible for the restructuring. The decision authorizing its sale is made by:

- i. Provincial Governor, in the case of companies under provincial jurisdiction
- ii. Minister responsible jointly with the Minister of Planning and Finance, in the case of companies nationwide
- iii. Prime-Minister, in the case of companies of the Council of Ministers or when the sale is made by different methods of tender.

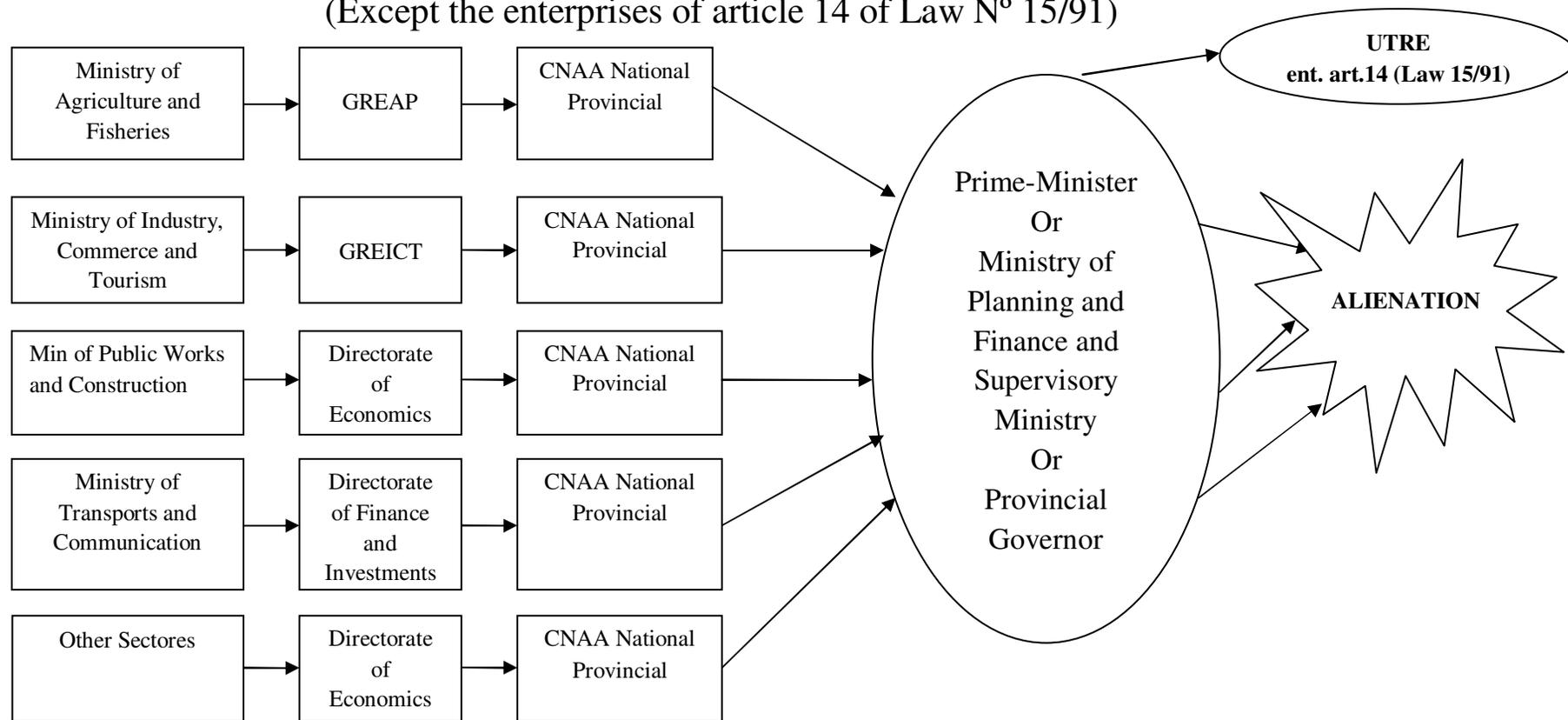
The Office of Corporate Restructuring of Industry, Trade and Tourism (GREICT) were responsible for supporting CNAAs and CPAAs in charge of the restructuring of SMEs at the Ministry of Industry, Commerce and Tourism (MICTUR).

The Office of Corporate Restructuring Agricultural and Fishery (GREAP) was the corresponding unit responsible for supporting CNAAs to CPAAs responsible for the restructuring of enterprises in the agro-livestock and fisheries. The CNAAs of other ministries were directly supported by the respective departments of economics and/or investments. The diagram 2, illustrates systematically the process of privatization for SMEs.

The privatization and restructuring program for SMEs targeting about 222 enterprises was complete by 1999. The government had majority ownership in 33 enterprises, of which: 10 public enterprises owned 100 percent by the government and 23 companies in which the state holds 51-95 percent of the capital.

# THE PROCESS OF PRIVATIZATION FOR SMALL AND MEDIUM ENTERPRISES

(Except the enterprises of article 14 of Law N° 15/91)



Definition of the sectoral programs  
 -classification of the juridical situation  
 -technical evaluation of the unit

-Representatives: Min. tutelary, MPF, BM  
 -preparation, realization and evaluation of the bid and negotiation with the investors

-Final decision  
 -Prime Minister, modality different from the public bid

Source: Metier (2003)

### 5.2.3. *Banking and Financial Sector*<sup>22</sup>

The political and economic crises in the 1980s also affected significantly the Mozambican banking sector. At this time the Mozambican banking sector was centralized. Until 1989, the banking sector in Mozambique was characterized by few commercial banks and about 95 percent of the bank activities were controlled by the state (Coscione, 2008). In addition, the banking system functioned as an operation channel of the state budget, and large proportion of the credit was granted to SOEs. The end of socialism and introduction of a market oriented economy, motivated the creation of an appropriate legal framework for the development of the banking and financial sector.

The implementation of the Economic Restructuring Program introduced several financial and banking sector reforms. One of the objectives of PRE was to provide solutions to problems and deficiencies of the financial sector. It also allowed foreign banks to invest in Mozambique. The major economic reform towards liberalization of financial and banking services was the separation of the commercial and central bank functions of Banco de Moçambique.<sup>23</sup> In 1992, *Banco de Moçambique* begins to solemnly have the function of a central bank, and all the functions of a commercial bank were transferred to the newly created *Banco Comercial de Moçambique* (BCM) with its own identity and management. The commercial bank was created with the objective to open the banking market to foreign investments (Cosions, 2008).

At the end of 2000-2001, the banking sector was affected by a crisis. During this crisis two of the major commercial banks *Banco Comercial de Moçambique* and *Banco Austral* were declared insolvent. The government through a bail-out operation worth \$128 million was able to recover the situation.

Along with the opening of several new commercial banks, for the implementation of the capital market in Mozambique, the government created the Installation Committee of the Stock Exchange for Mozambique, which worked with the private sector to create the first stock exchange in Mozambique in 1999.

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<sup>22</sup> Among others things, the PRE gradually led the economy to a more market oriented mechanism of price setting (Interest rates in 1994, exchange rate floating regime in 1996, most goods and services price in 1997 and bank privatization from 1996).

<sup>23</sup> Law No. 1/92 of 3<sup>rd</sup> January attributed the Central Bank the exclusive function of a Central Bank. The approval of law 15/99 - Law of Credit Institutions and Financial Societies.

## **6. The Results and Impact of Privatization in Mozambique**

The privatization process and its economic reforms have an interaction with the economic development that the country has experienced in the past years. A major constraint faced to address privatization issues in Mozambique, is the lack of adequate data on the quantitative impact of privatization. Several studies have been conducted but most of these cover the qualitative aspects of the privatization. Despite this shortcoming, an attempt has been made to present the statistical results of privatization in Mozambique and a brief analysis of its economic impact.

### **6.1. The Results of Privatization**

Privatization in Mozambique is considered to be one of the most successful in Africa. In fact, the privatization process has taken place in a large scale in terms of transaction, compared to rest of Africa (Castel-Branco and Hailu, 2001). Overall, privatization has proven its economic worth. Large proportion of the restructuring of enterprises took place in the years after the peace treaty.

An analysis of the first stage of privatization trends in Mozambique show that by the end of 1990s the Government of Mozambique generated about \$80.4 million from about 1254 transactions, representing just 42 percent percentage of total enterprises that have been restructured and privatised. This involved a large range of SOEs in both urban and rural areas, from high-technology industry to small rural tuck-shops.

Furthermore, new public enterprises were created with special attention to Mozambique Railways (CFM), Mozambique's Television (TVM), Mozambique's Radio (RM), Electricity of Mozambique (EDM), Telecommunications of Mozambique (TDM) and Mozambique Post office.

In terms of economic sectors, large proportion of restructured enterprises is in industry, commerce and tourism sector (49 percent), Agriculture (25 percent) and Construction (15 percent). Across geographical location the restructuring process has been unequally distributed, with strong concentration in urban areas. About 53 percent of the privatized enterprises were in Maputo, 13 percent in Sofala and 7.5 percent. The remaining 27.5 percent enterprises were distributed across all the other provinces.

Currently, the government is still aimed at reducing its participation in the private sector. Since the dismantlement of UTRE, the privatization process has been undertaken by IGEPE. This new privatization era has been characterized by much more activity, with the privatization of companies in the agriculture, aviation, energy, and ports sectors. Under the program conducted by IGEPE about 189 enterprises have been privatized.

## 6.2. The Impact of Privatization

Privatization was a central element of the economic reform in Mozambique during the 1990s. Yet, empirical evidence regarding the impact of privatization remains scarce. Since the studies by UTRE, GREICT and World Bank (1996), National Directorate of State Holding (1997) and UTRE and the commonwealth secretariat (1998) on the impact of privatization in the Mozambican economy, no other comprehensive post-privatization assessment has been conducted.<sup>24</sup>

Therefore, a major constraint faced in trying to evaluate the socio-economic impact of privatization in Mozambique is the lack of availability of adequate quantitative data about privatization or privatized enterprises. Although several studies have been conducted, most of them cover the qualitative issues of privatization with little emphasis on the quantitative analysis such as improved efficiency and performance of privatized enterprises.

Despite this shortcoming, this section aims at giving a broad overview of the impact of privatization in Mozambique, in the light of the recent development, and to derive some general trends and conclusions from the body of empirical evidence available up to date. Therefore, the analysis presented below may not only reflect the effect of privatization but a joint effect of other macroeconomic policies implemented.

### 6.2.1. Evaluation of the Impact of Privatization

As elsewhere, privatization policies in Mozambique were aimed at enhancing the efficiency and competitiveness of enterprises, improve productivity and attract investment. Overall, these objectives have been achieved (Metier, 2003).

On the basis of the available information the evaluation of the impact of privatization is analysed from the following perspectives: i) Enterprise Performance, ii) Labour Markets, iii) Investment and v) Government Finances.

### Enterprise Performance

Assessing post-privatization enterprise performance is a very challenging task. It requires knowledge about pre and post privatization performances or try to predict what would have happened in absence of privation under a set of reasonable assumptions. Nevertheless, the overall privatization results have been positive in the manufacturing industry.

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<sup>24</sup> In 1996 joint study by UTRE, GREICT and the World Bank covering a sample of 91 privatized enterprises, ii) a 1997 survey undertaken by the National Directorate of State Holding (DNP) on a sample of 374 privatized enterprises and iii) a 1998 survey by UTRE and the commonwealth secretariat on a sample of 20 large privatized enterprises.

From a business environment performance perspective, privatization appears to have been successful in revitalizing the enterprise sector in Mozambique (Buchs, 2003). Upon privatization the number of operating enterprises increased. The average number of business stalled and semi-paralyzed reduced from 58 percent to 13 percent in 1996. In addition, the number of operating businesses has increased significantly from 41 percent to 77 percent of production units, also increasing the level of capacity utilization. Currently, the private sector is constituted by approximately 28 870 enterprises of which 98.6 percent are Micro, Small and Mediums Enterprises (MSMEs).

Performance wise enterprises in the manufacturing sector have registered an improvement. The overall assessment of firm's profitability shows that the level of actual sales doubled as a whole after privatization (UTRE, 1998). An impact study over 91 firms across the Mozambican enterprise sector found that following privatization, most of the enterprises in the sample could be characterized as showing an overall improvement in their performance based on increases in sales and production levels. Another study covering 152 firms in the manufacturing sector between 1992 and 1998 found similar results in terms of labour productivity<sup>25</sup>, investment and sales growth, although new entrants seemed to be better than privatized firms in terms of sales growth (Biggs *et al*, 1999). A flagship of the privatization program is that of creation of the brewery company Cervejas de Moçambique (CDM), following the privatization of the three local breweries in 1995, leading to triplication of production between 1995 and 1998 (Busch, 2003).

One of the major failures of the program is certainly that of the privatization of Banco Comercial de Moçambique in 1996, which was completed despite major concerns about the only bidder, a Portuguese consortium. Soon after, the bank was in trouble because of fraud, large loans to connected parties and problems with the pre-privatization portfolio resulting from poor regulations and lax supervision and political pressure to lend to "well connected" parties, and had to be recapitalized in 2001.

The above results did not apply to firms across all economic sectors. The lack of improvement in efficiency and productivity was explained by the poor handling of the privatization prices itself. Most of the enterprises were sold to local buyers, most of which lacked the ability to run such enterprises.

### **Labour Markets/Employment**

Privatization reduces overstaffing and leads to layoffs. It replaces political and social objectives with profit maximization. In most cases, privatization makes companies more efficient and

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<sup>25</sup> Information from firm level performance was gathered from enterprise surveys (World Bank, 1998; World Bank, 2003; DNEAP, 2006; World Bank, 2009).

profitable by reducing the size of the labour force. Governments lay off workers when they prepare large, poorly performing state companies for privatization in order to make them more attractive and to generate higher revenues (Bhatia and White, 1998). Once privatized, the demands of efficiency and competition frequently force the new owners to lay off more workers.

In the case of Mozambique, the overall effect of privatization on employment was positive. Although the privatization process was turmoil, about 40 percent more jobs were created by the end of 1999. In the period immediately after the privatization the level of employment declined, because many SOEs (especially large ones) introduced policies to reduce the workforce, due to the level of overstaffing. In addition, the civil war and the consequent resulting economic crisis lead to an additional decrease in employment rate. However, during the post-privatization period many enterprises reopened (mostly SMEs) many employees benefited directly from the new jobs created, reversing the negative trend by boosting in employment.

However, the above finding does not hold for all period subsequent privatization or for all economic sectors. The overall growth rate of employment in the manufacturing sector was flat during 1992-1997 (Word Bank, 1998). The employment rate declined in the period immediately after privatization (1992-1995) achieving a growth rate of about -2.1 and gradually increasing during the period of recovery, registering a growth of 0.8 and 1.4 during 195-1996 and 1996-1997, respectively.

Privatization of SOEs generated an expansion of activities, caused by the creation of enterprises with new ownership and management, also accompanied by the development and growth of the informal activity, as an absorption factor and source of income for many unemployed workers.<sup>26</sup>

The GoM has complemented the privatization process with sound macroeconomic policy to promote employment and provision of social safety net in short-run. Labour regulation have been very restrictive and hampered employment in the formal sector. The new labour legislation introduced in 2007 brought about major changes in labour regulation for the private sector, especially in terms of labour flexibility to hiring and firing workers (World Bank, 2008)

### **Government Finance<sup>27</sup>**

Privatization should improve government's finance by increasing revenue from the sale of assets and shares of businesses, reducing the need for subsidies and by increasing tax revenues as a result of improved efficiency and productivity of enterprise.

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<sup>26</sup>It is worth noting that the restricted and isolated assessment to privatized enterprises, of the impact of privatization on employment does not necessarily show what happened in the economy and society as a whole.

<sup>27</sup> However it is not possible to assess the impact of privatization on the government finance, because information on government revenue prior to privatization is unavailable

During the period of 1987-1997 privatization proceeds amounted to about \$80 million, contributing directly to Government Budget. The total amount of disposal of enterprises amounted to 191.6 million, however only 80.4 million had been paid by the end of 1997, contributed strongly for the progressive equilibrium of the public finance.<sup>28</sup> In terms of the corresponding value of collections, it should be noted that, from the restructuring of large enterprises, was raised in the state coffers, \$64 million paid in cash at the time of award. The low level of recoveries made to date in November 1997 reflects mainly the situation of deferred payments on SMEs mostly negotiated with domestic investors.

The value of taxes paid to the State increased and the direct and indirect subsidies to the enterprises reduced. A good example of this is the company Cervejas de Moçambique (CDM) a brewer producing relatively cheap local beer, which is available all over southern and central Mozambique, and has destroyed the once thriving trade in smuggled South African beer. The government benefitted from the taxes paid by the breweries rose by 700 per cent. By 1998, CDM provided about 5 percent of total tax revenue (UN, 2000)

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<sup>28</sup> See Metier (2003)

## 7. Conclusions

Economic reforms and privatization of State-Owned Enterprises have been the focus for bringing economic stability. In developing countries has been promoted in the belief that it promotes efficiency and stimulates economic growth, thereby reinforcing macroeconomic adjustment and bringing economic stability. This study looks at the privatization process in Mozambique since 1986. The objective of the study was to analyse the privatization process in Mozambique and evaluate its economic impact by pulling together a synthesis of available research.

During the initial years, privatization in Mozambique has primarily been characterized by activities to make companies better acquainted with competitive mechanism within a market economy rather than to institute direct private ownership. The process of transforming state entities to private one has been intensified only after the implementation of major legal framework in 1989, subsequent to pressure imposed by the World Bank and IMF for fast privatization to advocate private ownership as an instrument for development, through the conditioning of foreign aid to the implementation of such policies.

In general, the Mozambican economy has undergone significant improvement since PRE and privatization. Overall goals of privatization set by government have been achieved. The government has been able to bring about an improvement in economic growth and macroeconomic stability. Through privatization, Mozambique achieved an expanded and more dynamic private sector, more efficient and effective infrastructure provision and increased investment, both domestic and foreign.

Privatization was beneficial for Mozambique. The beneficial results of privatization can be synthesized as follows: i) improved enterprise performance and ii) wider access to investment market. In terms of enterprise performance, efficiency dispersion is relatively high. In other words, large set of relatively inefficient firms are able to stay in business among highly efficient ones. The lack of technology and poor quality of labour force human capital are the main causes leading to a positive but weak improvement in performance. In addition, high degradable infrastructures, rigid labour laws, lack of access to finance and high cost of financial resources are also some of the causes of differences in efficiency.

The severe crisis facing the economy has hampered higher private involvement. Other problem related to the process has been the lack of well-defined strategies to help the newly privatized enterprises. The implementation and transparency of the privatization strategy were problematic. Privatization was delayed by lobbying and competition for cheap state assets, ambiguities in the criteria for selecting buyers, together with financial and managerial weaknesses among enterprises.

Finally, at this stage very little can be about the success or failure of privatization in Mozambique, unless better information is collected. Ideally, the privatized enterprises should be

revisited in order to accurately evaluate their performance. The challenge of the Mozambican government is to implement a system for monitoring and evaluation of private sector, for accurate and continuous assessment of private sector dynamics.

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