

Policybrief

No. 1, 2019

The Role of State-Owned Enterprises in Industrialization in Tanzania: Lessons from East Asian Economies

■ Dr. Josaphat Kweka

Inspired by the success of countries in East Asia, the Government of Tanzania is aggressively pursuing industrialization as a strategy to accelerate socio-economic development, create jobs and substantially reduce poverty. Notably, many economies in that region achieved a high level of industrialization and economic transformation through the participation of a large state-owned enterprises (SOEs) sector. This leads to the question: What role can SOEs play to support industrialization in Tanzania?

To stimulate and exchange views on this critical issue, the UONGOZI Institute in collaboration with the Office of the Treasury Registrar within the Ministry of Finance and Planning convened a roundtable policy forum in July 2018. This brief summarizes the key messages and policy recommendations from the meeting. In particular, delegates advised that, for SOEs to contribute meaningfully to industrialization in Tanzania, their role within the country's current development context needs to be re-thought and necessary reforms implemented, including formulating policy guidelines to address the prevailing governance and operational challenges affecting SOEs' performance.

Introduction

To realize its vision of becoming a middle-income country by 2025, the Tanzanian government through its Five Year Development Plan II (2016/17-2020/21) has prioritized industrialization as the key driver of economic transformation. However, despite the priority attached to industrialization, the structure of the economy shows a manufacturing deficit. For instance, to date, the manufacturing sector has played a much smaller role in driving growth and job creation, contributing less than 10% of GDP and employing around 3% of the labour force.

In many countries, particularly in East Asia, state-owned enterprises have been critical stakeholders responsible for translating national industrialization agendas into tangible results. Therefore, the UONGOZI Institute, in collaboration with the Office of the Treasury Registrar in the Ministry of Finance and Planning organized a roundtable policy forum to discuss the role of SOEs in Tanzania. The dialogue examined how SOEs have facilitated the industrialization agenda in other countries, and how SOEs can take advantage of opportunities and meet the challenges emerging during the process of

industrialization. The roundtable was held on 10 July 2018. The Hon. Dr. Philip Mpango (MP), Minister of Finance and Planning officiated at the event and the keynote address was delivered by **Dr. John Page**, Senior Fellow in the *Global Economy and Development Program* at the *Brookings Institution* in Washington, D.C. Key messages and policy recommendations emerging from the forum are summarized below.

In the past, SOEs were seen as barriers to growth; today, SOEs are being considered as levers for development.

Growth in SOEs is a global phenomenon, but countries differ on the extent they have harnessed the sector to support economic transformation. A recent study (PwC, 2015) shows that the proportion of SOEs among Fortune Global 500 corporations has grown from 9% in 2005 to 23% in 2014, including a greater presence in the top rankings, largely driven by China. However, the role of SOEs varies significantly between countries. For instance, the contribution of SOEs to GDP ranges from 2% in Indonesia to over 33% in Vietnam.

Many East Asian economies achieved success with a large SOE sector.

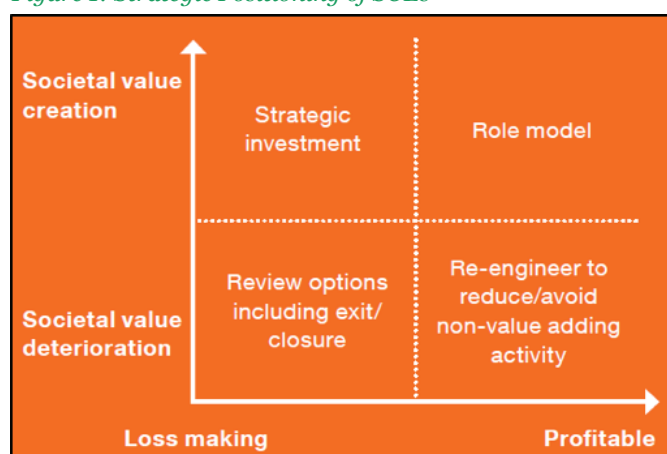
SOEs were key drivers of economic development in East Asia. The strategies of individual countries in leveraging SOEs varied considerably but some elements were common across all countries.

These included:

i. Gradualism. A pragmatic approach to economic reform was adopted, that included moving gradually from state-based to market-based economies. Importantly, countries put in place frameworks to guide decision-making for divestiture and investment in SOEs that balanced the societal value of investments with their commercial profitability (Figure 1). Clearly, the Figure shows two motivations for guiding Governments in making strategic policy reforms on the role of SOEs in the economy: that is making either social value or profit or both. On one hand, a SOEs may be loss making but the State keeps it if its social value is notably high (i.e. strategic investments). The Government is advised to reform/re-engineer SOEs which are highly profitable but with very low social value. On the

other hand, the Government should exist/abandon or divest SOEs which are both loss making with low social value; and embrace (promote) those that are both highly profitable with significant social value as role models.

Figure 1: Strategic Positioning of SOEs



ii. A “back the winners” approach. State support was focused on strategic sectors and enterprises that contributed to transforming the economy. Where necessary, hard reforms were adopted which allowed divestiture to foreign direct investment (FDI) of poorly performing SOEs with the government taking majority or minority shares.

iii. Alignment and partnership with the private sector. The private sector was viewed as a critical partner in formulating and implementing national industrialization strategies. Underlying this collaboration was the strong need for public-private sector dialogue to ensure that activities of the two sectors were coherent not contradictory. In Singapore, SOEs and foreign direct investment (FDI) were combined as government-linked corporations (GLCs). In effect, the government used to run Singapore as a business entity.

iv. Robust performance monitoring and evaluation. Results-based management (RBM) coupled with good corporate governance were adopted to ensure the accountability of SOEs.

v. Dynamism. The roles and tactics of SOEs evolved over time as economies developed. In most cases, this evolution meant devolving some activities to be run commercially by the private sector after achieving a significant level of competitiveness.

In Tanzania, SOEs play an important role but are not dominant in the economy.

Currently, around 270 fully registered SOEs are operating in Tanzania, managed under the Office of the Treasury Registrar. They are clustered around major sectors of the economy, including power, transportation, water, ICT, land and housing, and financing. Of these entities, the Government has full ownership of 232 enterprises. In total, the investment in SOEs represents about 10% of GDP. In value terms, about 60% of Government investment is held in 10 corporations, of which four are service providers:

Reli Asset Holding Company (RAHCO) (now transformed to Tanzania Railway Corporation), Tanzania Electric Supply Company (TANESCO), Tanzania Ports Authority (TPA) and the National Housing Corporation (NHC).

Several important corporations, such as the Tanzania Petroleum Development Corporation (TPDC) and Air Tanzania are not in the top ten.

A number of challenges limit the role of SOEs in industrialization in Tanzania

Forum participants identified the following challenges that negatively impact SOEs in Tanzania:

i. Financial viability. SOEs have been under-capitalized for a long time.

ii. Governance. Some SOEs do not have Boards of Directors, which limits their decision-making powers. Also, decision-making processes in most SOEs are too bureaucratic, limiting the extent to which SOEs can become competitive and responsive.

iii. Independence. Participants remarked strongly on the lack of autonomy in running SOEs; in most cases, executive appointments are politically motivated rather than based on professional competencies.

iv. Incentive framework. Remuneration and

incentive schemes for senior executives in SOEs are not competitive with the private sector, hence, it is difficult to attract highly-skilled professionals.

v. Strategic direction, in that, the Government should distinguish the activities/sectors that are best run by the private sector from those that are best run by SOEs (including sectors of strategic importance).

Policy recommendations

Participants highlighted several important lessons that Tanzania can apply from the experience of East Asian countries. To improve the sector, the Government was advised to:

i. Improve accountability and reporting on performance evaluation of SOEs. The management of SOEs needs to be dissociated

The management of SOEs needs to be dissociated from political interference by establishing a strong, independent institution responsible for managing the sector, and robust performance management and reporting systems need to be instituted to improve accountability.

ii. Clarify competition between SOEs and private sector firms. The government needs to enhance the complementarity between the private sector and SOEs, and ensure a level playing field between the two. In principle, during the process of industrialization, SOEs can compete with private operators, but it is important to develop national guidelines that distinguish the two in terms of their roles and activities.

iii. Develop interventions to increase the productivity of SOEs. Productivity is a composite

outcome of many different factors, from factors of production to societal values and attitudes. Therefore, influencing and improving productivity will require overarching interventions. Of these, agglomeration, i.e., leveraging industrial clusters, was considered the most important. The Government also needs to conduct feasibility studies to confirm the financial viability of enterprises prior to further investment.

iv. Improve implementation capacity. For SOEs to contribute meaningfully to Tanzania's industrialization and economic transformation, critical institutional requirements (which are notably missing) need to be met, particularly the adoption of good corporate governance and the provision of adequate financial and human resources.

Conclusion

Though not as economically dominant as their counterparts in East Asia, SOEs in Tanzania have the potential to play a significant role in promoting industrialization if they can accurately translate the country's development agenda into practice. To achieve this, the Government will need to elucidate the national vision, promote national dialogue on its desired transformation strategy, and build effective support programmes for its implementation. All stakeholders must be involved. Vitaly, to improve planning for the future, the Government will need to be open and transparent about things that did not work in the past and why, and implement the necessary reforms to address the governance and operational challenges affecting the performance of state-owned enterprises.

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