Background to the Study

- Follow-on study to Finding Balance 2009 which focused on Fiji, Samoa and Tonga
- Finding Balance 2011 adds Marshall Islands and Solomon Islands to the benchmarking analysis, and includes financial results through FY2009
- The study analyzes four core dimensions of SOE performance:
  - Financial
  - Legal
  - Governance
  - Monitoring frameworks

Recent SOE Reform Progress

- Fiji:
  - ✓ liquidation of Fiji Ships and Heavy Industries Limited
  - ✓ corporatization of the Water Authority
- RMI:
  - ✓ 2010 cabinet decisions to restructure the Marshalls Energy Company and to implement a series of good practice principles applicable throughout the SOE portfolio, placing them on a more commercial footing
- Samoa:
  - ✓ the successful privatization of SBC and SamoaTel
  - ✓ appointment of an independent director selection committee in April 2010

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Recent SOE Reform Progress

- Solomon Islands:
  - ✓ promulgation of SOE regulations to support the 2007 SOE Act
  - ✓ privatization of Home Finance Limited and Sasape Marina
  - ✓ restructuring of the boards of three large SOEs;

- Tonga:
  - ✓ privatization of Leiola Duty Free and Tonga Machinery Pool
  - ✓ restructuring of 10 SOE boards
  - ✓ publication of the financial results of the SOEs in local newspapers
  - ✓ implementation of rationalization strategies for all but three of the SOEs;
  - ✓ development and implementation of a director performance evaluation process
  - ✓ adoption of a robust Public Enterprise Amendment Act

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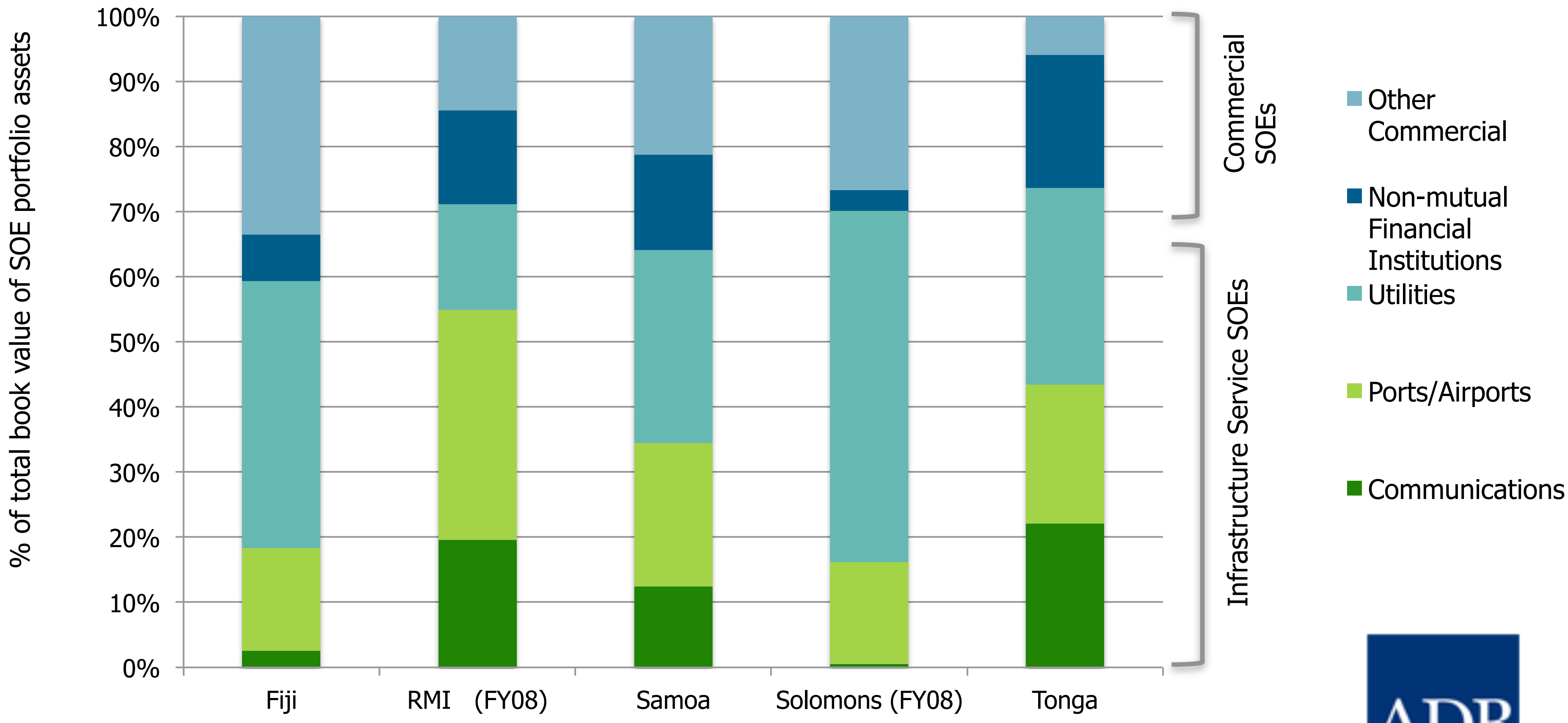
Common characteristics of SOE sectors in each country

- SOE reform has been underway for at least 10 years in each country
- SOE legislation largely based on New Zealand model
- Similar SOE portfolio composition:
  - ✓ Mix of infrastructure service SOEs and commercial SOEs

Composition of SOE portfolios

- Infrastructure SOEs represent between 59%-73% of total portfolio assets in FY09

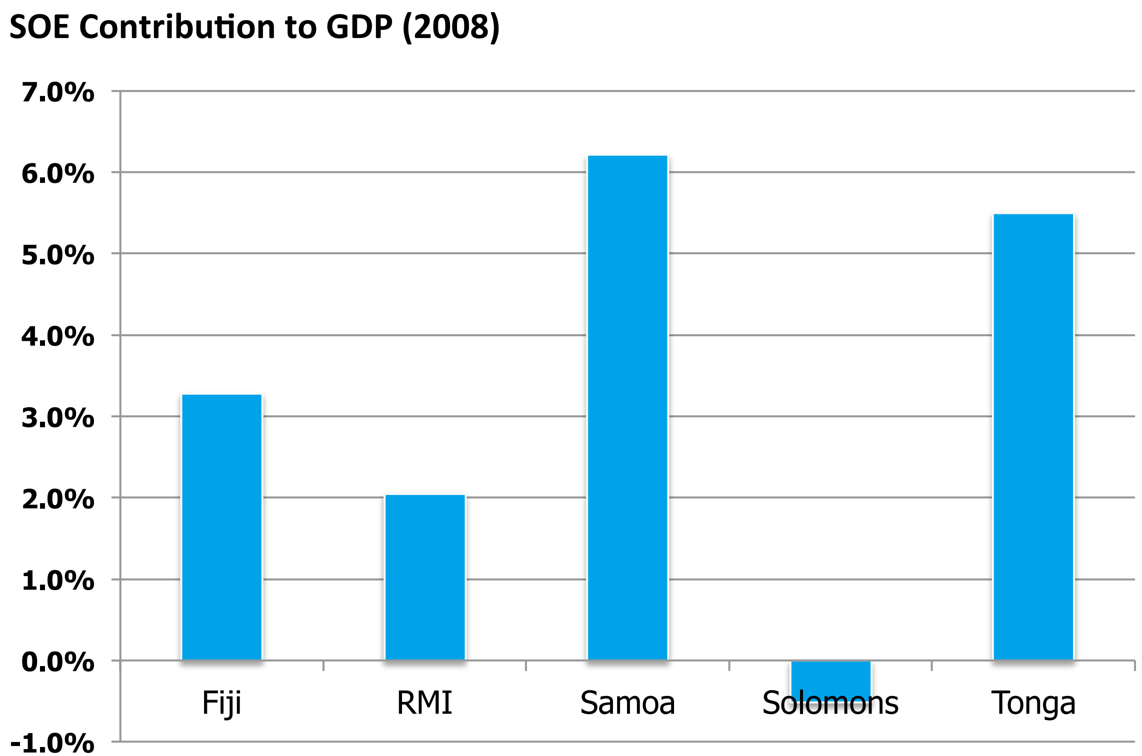


Common findings

- SOEs negatively impact economic growth in all five countries:
  - ✓ Absorb significant amounts of scarce capital stock, yet contribute very little to GDP
  - ✓ Crowd out the private sector, by competing on an unequal basis
  - ✓ Absorb government funds that could otherwise be spent on vital social sectors such as health and education

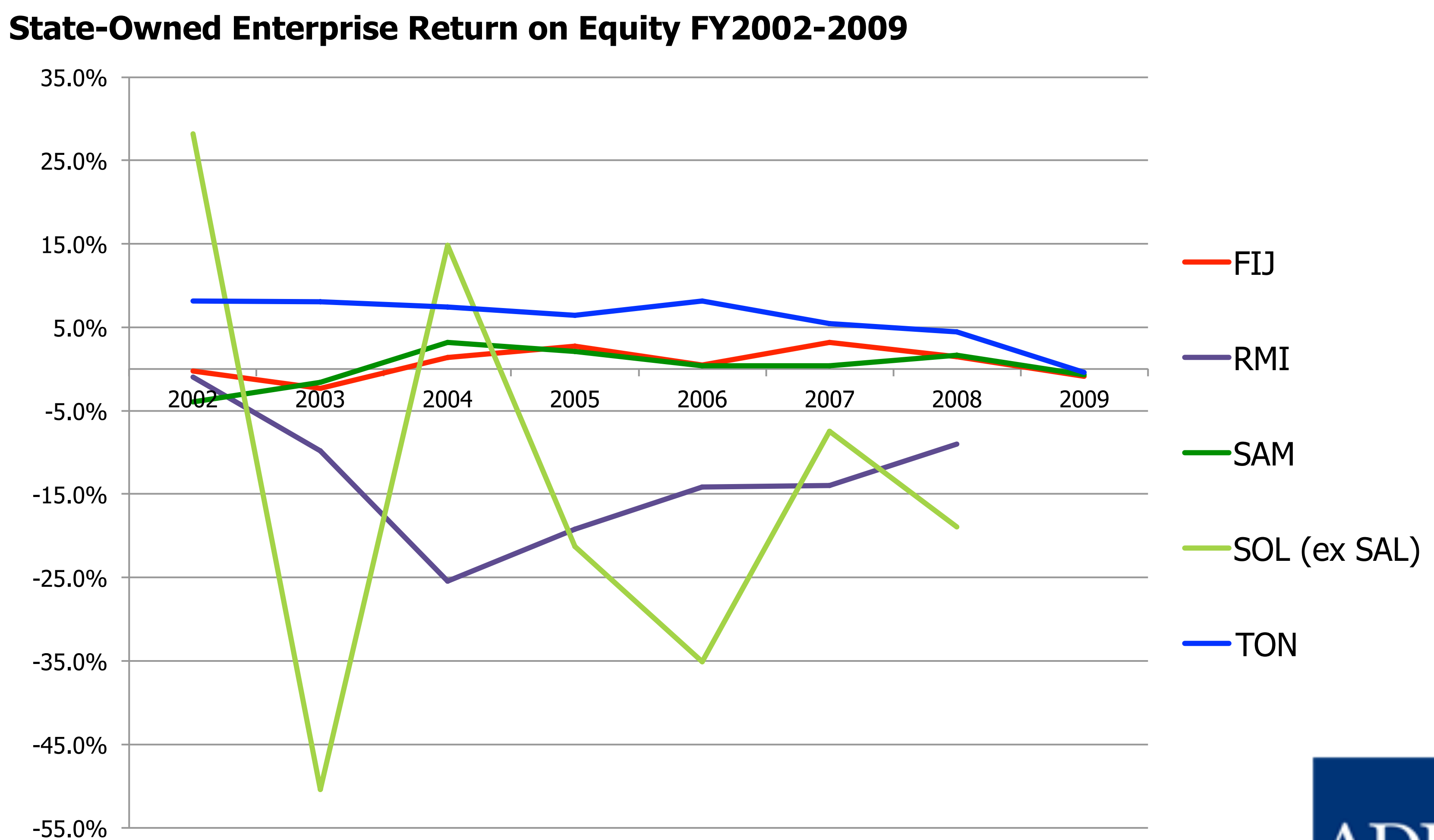
Economic Impact of SOEs

- SOEs represent up to 31% of total fixed assets in each country, while contributing comparatively little to GDP



Contribution to GDP is calculated by adding total wage expenditure to EBITDA and dividing by GDP

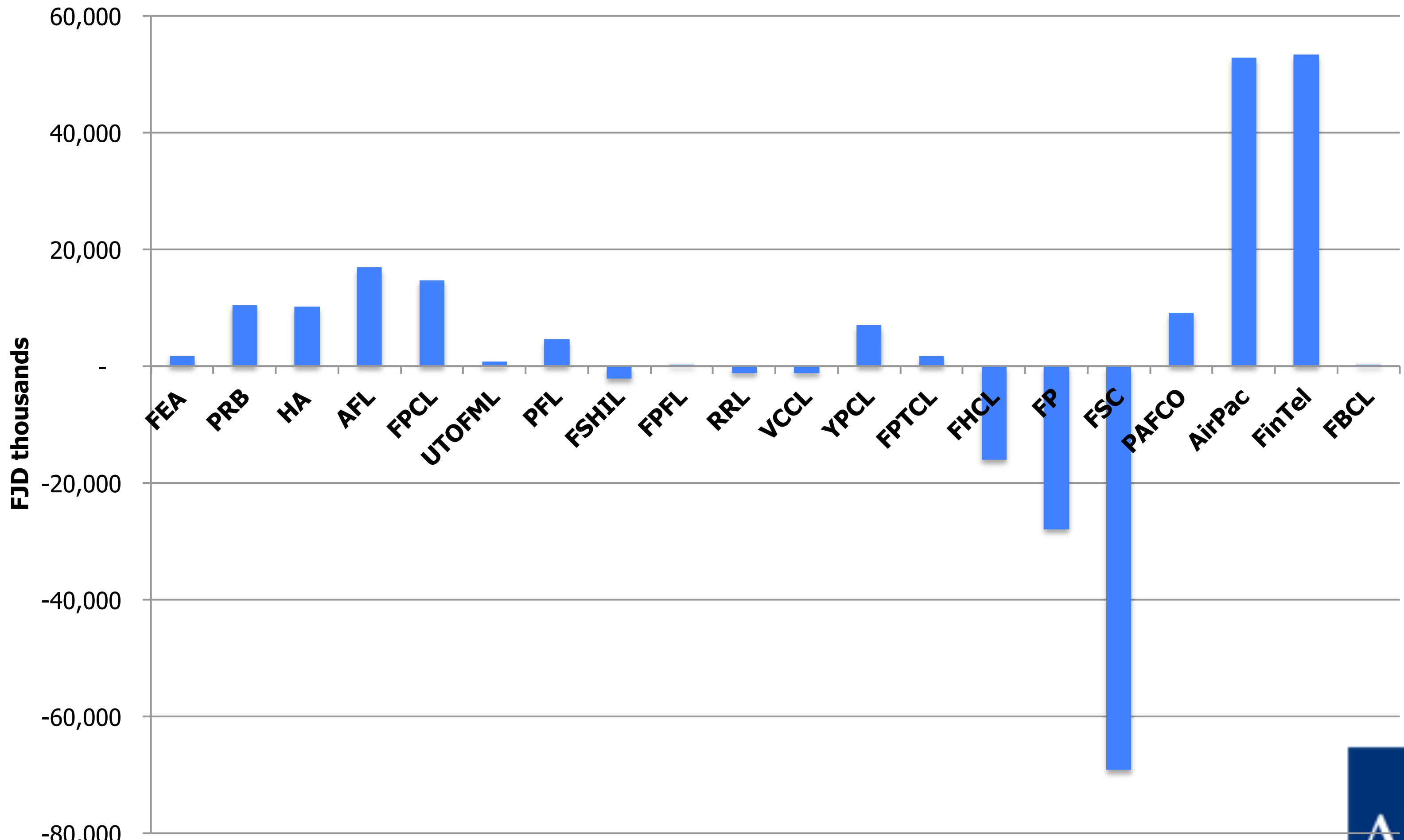
Financial Performance of SOEs: ROE



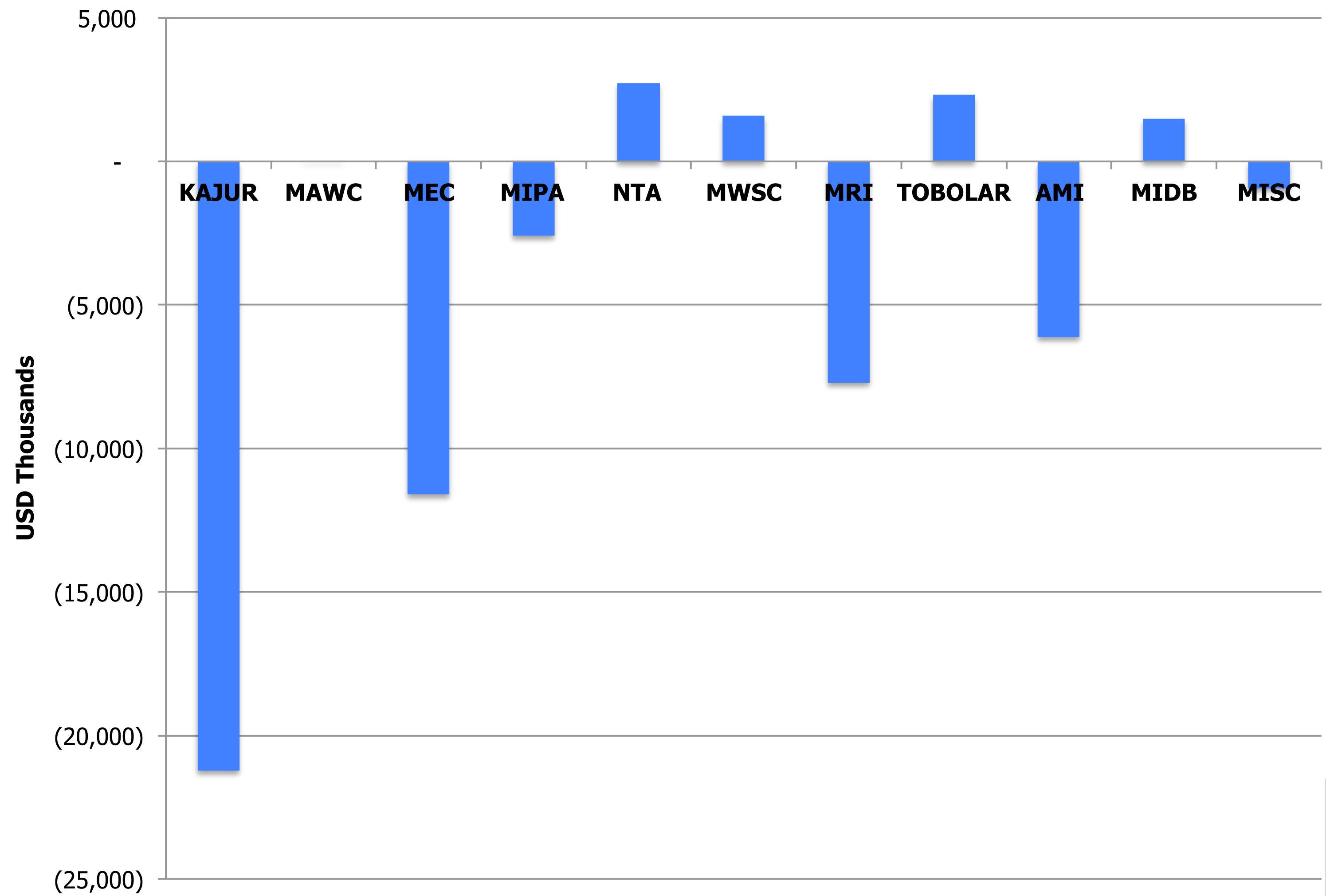
Financial Performance of SOEs: ROA

State-Owned Enterprise Return on Assets FY2002-2009

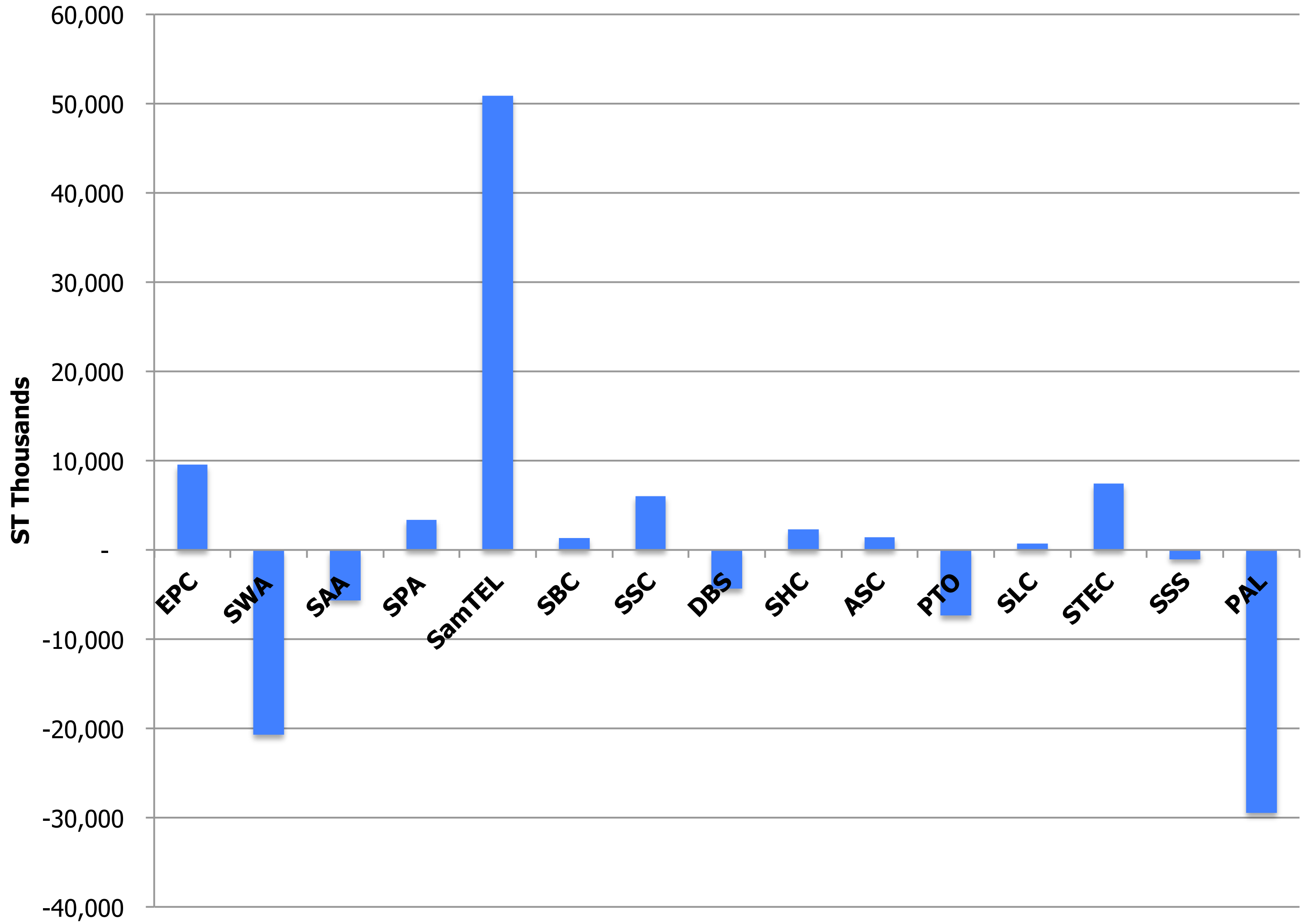
Fiji: SOE Net Profit FY02-09



RMI: SOE Net Profit FY02-08



Samoa: SOE Net Profit FY02-09



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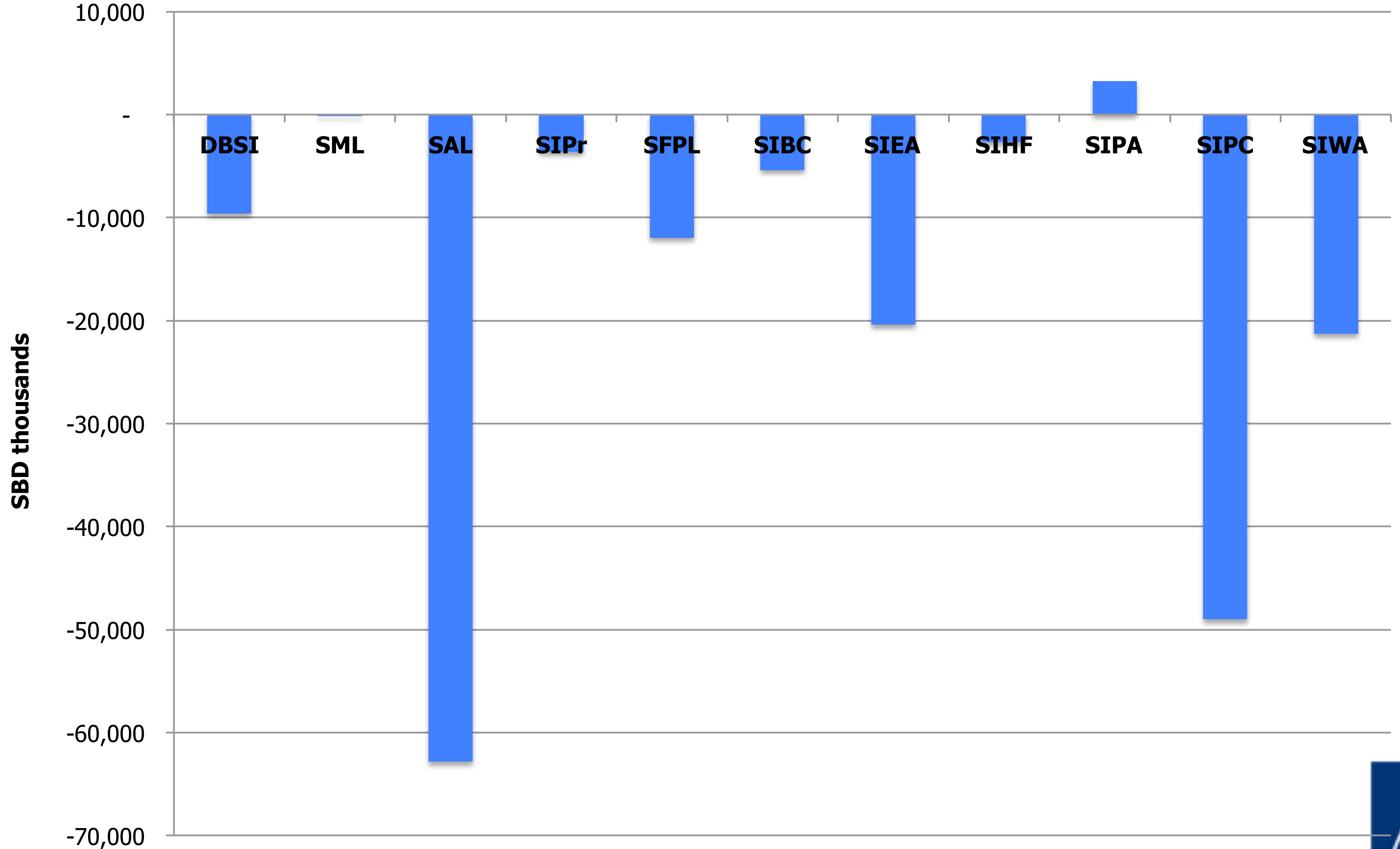
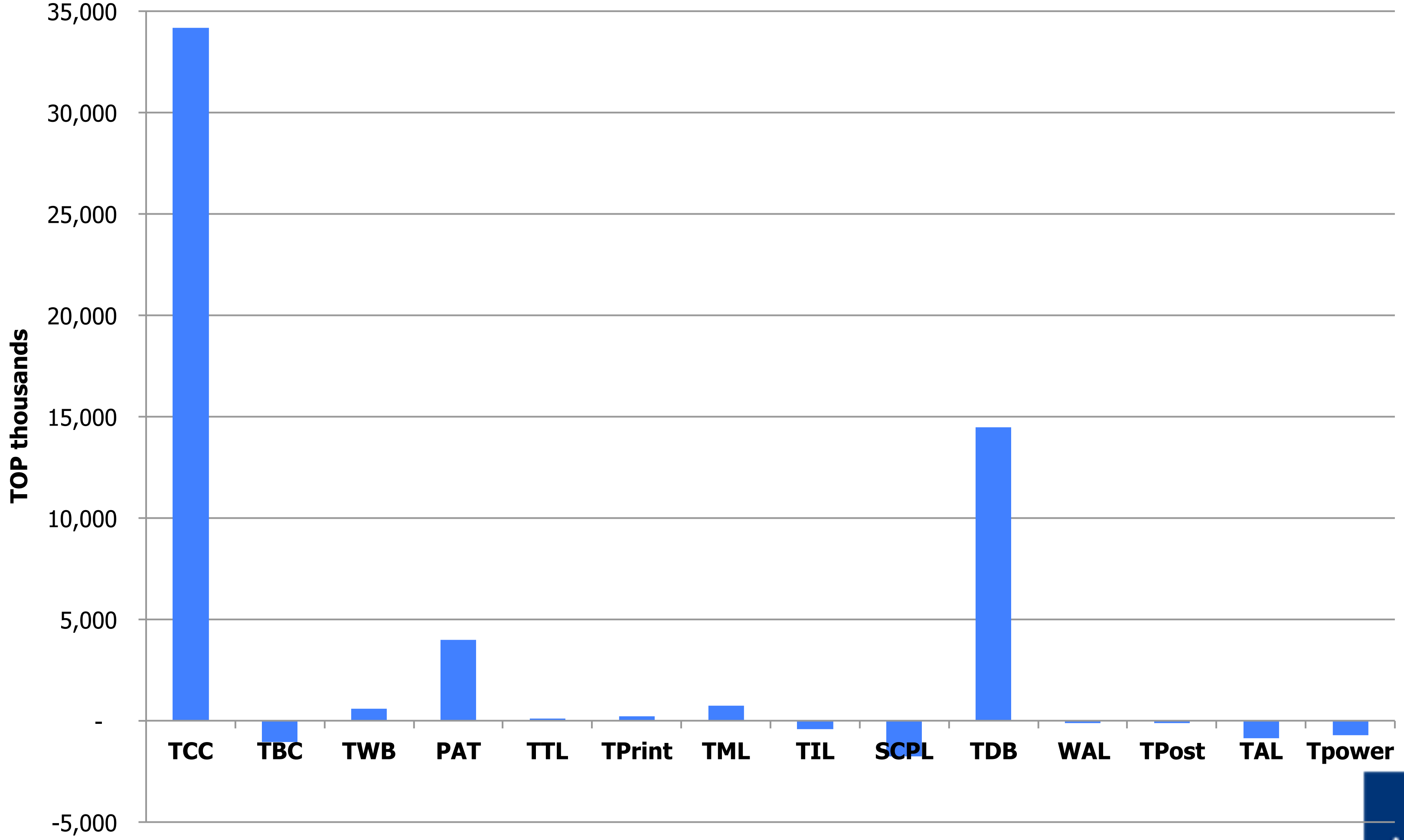
Solomon Islands: SOE Net Profit FY02-08



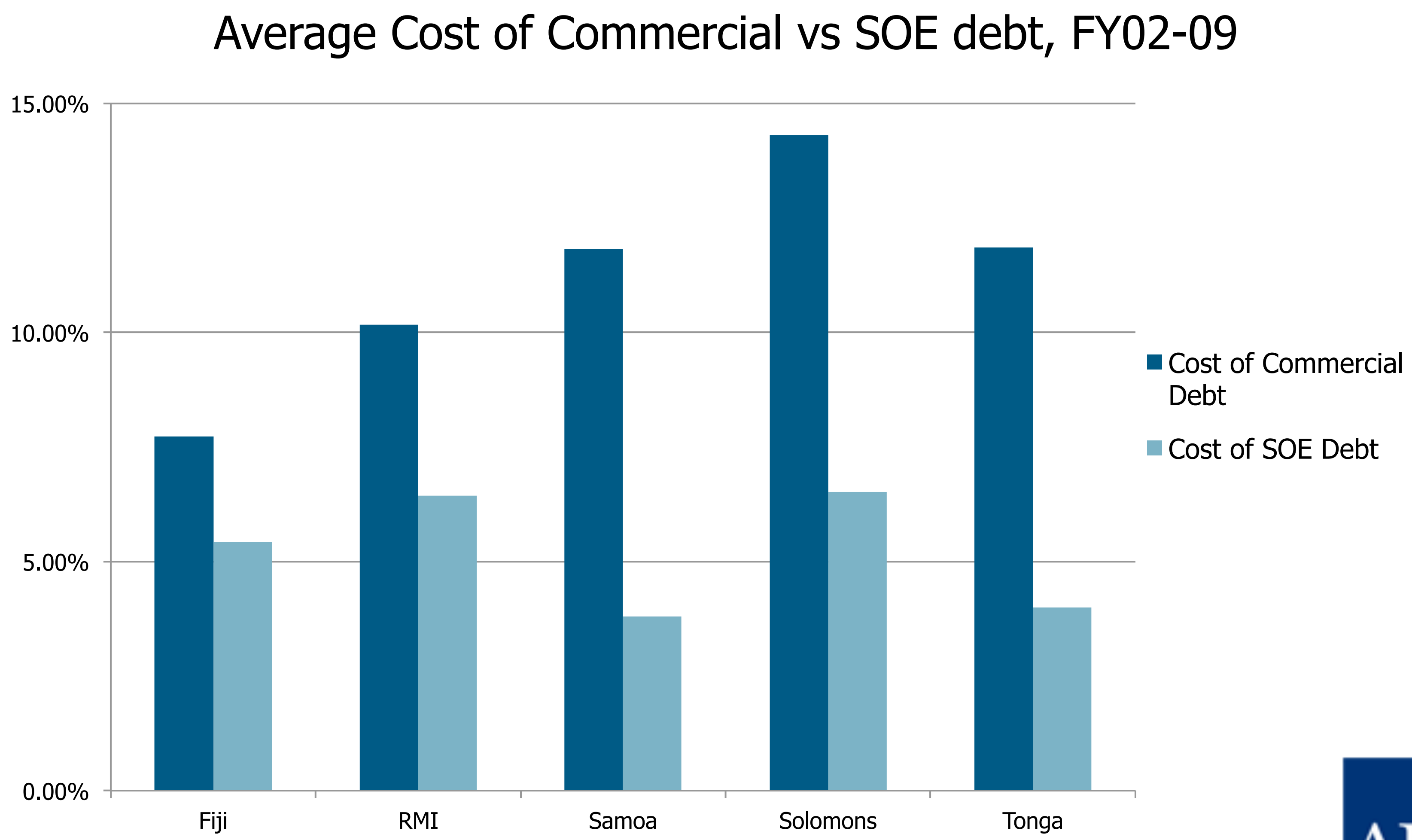
Tonga: SOE Net Profit FY02-09



Portfolio Comparators

(millions USD)	**Solomon Islands**	**Tonga**	**Samoa**	**Fiji**	**RMI**
Total SOE Assets FY08/09	$75	$144	$618	$1,231	$116
Aggregate Net Profit FY02-09	($24)	$25	$5.6	$33	($42)

Cost of Debt



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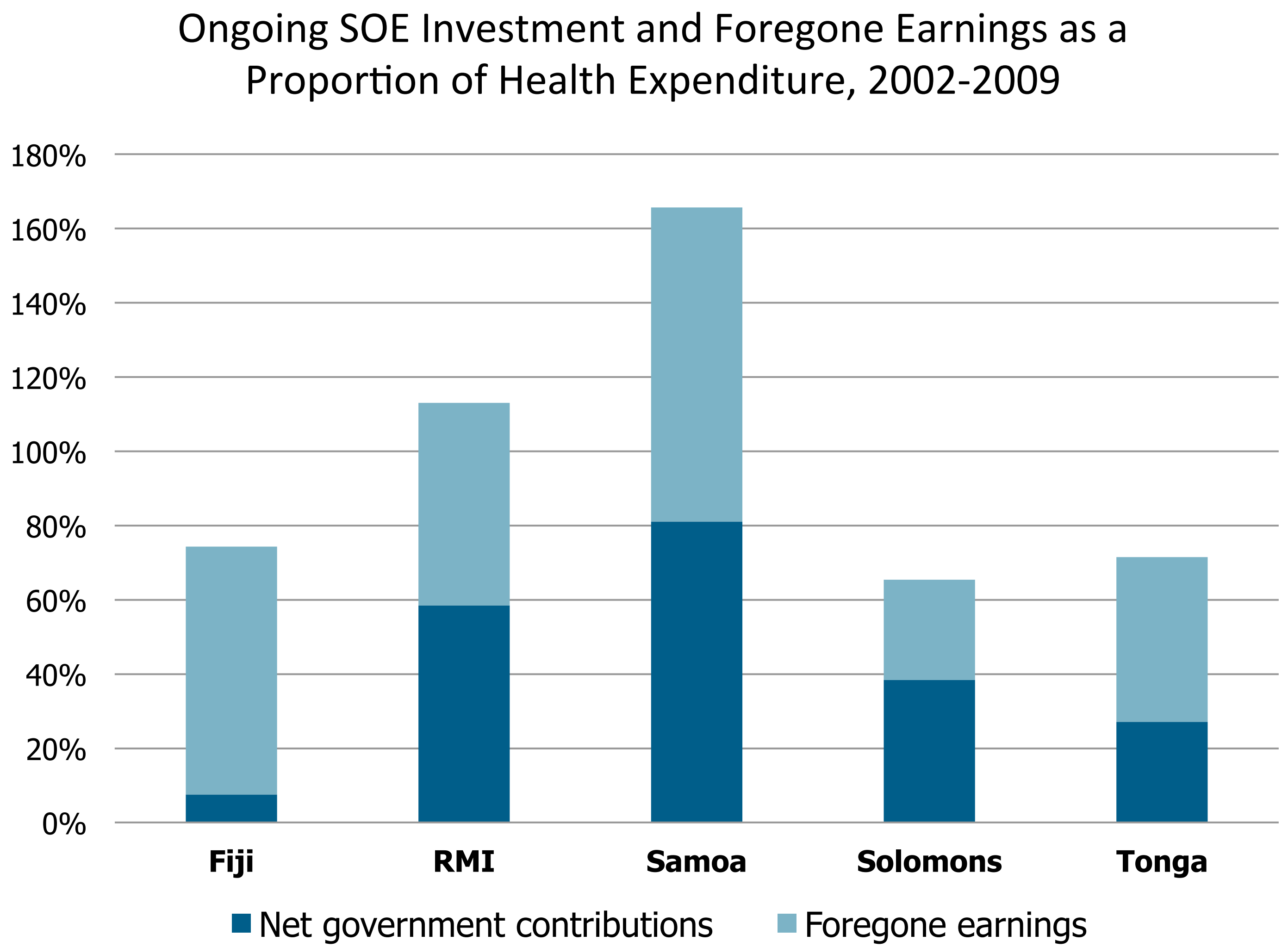
Fiscal Impact of SOEs



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Legislation - Overview

- SOE legislation in Fiji, Samoa, Solomon Islands and Tonga is based on the NZ legislation
- Marshall Islands has no SOE Act
- SOE Act in Fiji, Samoa, Solomon Islands and Tonga all contain the principle objective that every SOE must operate as a successful business.
- Samoan legislation was the most robust, but now overtaken by Solomon Islands and Tonga
- Fijian legislation is the oldest and could be strengthened
- SOE legislation is supported by Companies Act
  - ✓ Samoan, Solomon Islands & Tongan Companies Act based on NZ 1993 Act, which is seen as best practice
  - ✓ Fijian Companies Act is being updated

Legislation – Key Observations

- Fiji
  - ✓ Weak governance provisions exacerbated by outdated Companies Act
  - ✓ Strong provisions dealing with establishing SOEs, rights and obligations of minister and reporting requirements
- Samoa
  - ✓ Legislation very thorough and has excellent provisions dealing with directors duties and CSOs, but is not enforced
  - ✓ If Samoa were to meet the requirements of the Act, SOE performance would improve
- Solomon Islands
  - ✓ Based on Samoa SOE Act but with innovative enhancements
  - ✓ Enacted in 2009; limited implementation track record
- Tonga
  - ✓ Prior to 2009, practice exceeded legislative requirements
  - ✓ 2010 SOE Amendment Act has brought legislation in line with practice with additional innovations – public disclosure; holding company

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Legislation – Key Findings

- No direct causal link between robust legislation and good performance
- Clear causal link between the absence of effective SOE legislation and poor financial performance
- Robust legislation without enforcement produces similar financial outcomes as no SOE legislation
- SOE legislation is continuing to evolve with both Tonga and Solomon Islands introducing innovations
  - ✓ Public disclosure of SCI, annual accounts and director appointments (SI)
  - ✓ Codified skills based director selection process (SI)
  - ✓ Public disclosure of summary of SCI, annual accounts and key performance indicators (Tonga)
  - ✓ Codified requirement that CSOs be priced to cover the cost of capital (Tonga)

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Governance - Overview

- Ministers, MPs and public servants sit on SOE boards in Marshall Islands, Samoa, Solomon Islands and Tonga
- Fiji : monitoring staff sit as observers and public servants as directors
- Samoan and Solomon Islands SOE Acts severely limit the ability to appoint MPs as SOE directors - new Tongan Act prohibits it
- Solomon Is Act establishes best practice in board selection and appointment, Fiji is weakest
- Samoa now removing ministers and public servants from SOE boards

➔ SOE performance would improve with greater accountability for director and CEO performance

Governance – composition of boards

	SI	Tonga	Samoa	Fiji	RMI
No of SOEs	13	13	19	18	11
No of Directors	71	59	176	58	69
Politicians serving as directors	11	2	20	0	22
Public servants serving as directors	19	4	66	14	13
% Public servants and politicians	42%	10%	48%	24%	51%
Politician or public servants serving as chair	6	2	17	6	10

Governance – Key Findings

- Having ministers and public servants on boards creates conflicts of interest
- Having SOE monitoring staff sit as observers also creates conflict and confusion
- Important to ensure separation between minister as owner and board as manager – deemed directors
- Governments should appoint professional directors
- Solomon Islands skills based selection process is leading edge in the Pacific
- Tonga's development of job descriptions and a director performance review process should be adopted by other countries
- Important to continue to train and educate directors

➔ Close correlation between governance practice and performance

Monitoring - Overview

- Tonga and Fiji have separate monitoring ministries
- Monitoring processes very similar in Fiji, Samoa, Solomon Is and Tonga
- Marshall Islands has no central monitor and little concept of the “ownership” interest
- Samoa and Fiji use combination of Statements of Corporate Intent (SCI) and Corporate plan while Tonga relies totally on SCI (now called Business Plan)
- Fiji and Samoa use standing parliamentary committee to assist in reviewing SOE performance
- Tonga has published key SOE performance indicators for FY 2008 and 2009

Monitoring - Overview

	Solomon Is	Tonga	Samoa	Fiji (MPE)	Fiji (MoF)
No of SOEs	11	16	27	16	5
Staff	3	4	7	4	7
SOE/Staff	3.67	4	3.9	4	0.71
Total Assets (millions USD)	$75	$144	$618	$885	$346
Asset Value per Staff member	$25	$36	$88	$177	$49
Institutional arrangement	Unit in Ministry of Finance	Ministry	Unit in Ministry of Finance	Ministry	Ministry

Monitoring - Key Findings

- Monitoring structure does not seem to significantly impact on SOE performance
- Ineffective monitoring does adversely impact on SOE performance
- Merit in monitoring agency reporting directly to responsible minister
- Presence of ministers and public servants on boards compromises effective monitoring
- Should be clear consequences for non-performance
- There should be greater public disclosure of key SOE performance indicators

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Monitoring - Key Findings

- All countries would benefit from:
  - ✓ clearer expectations on content of corporate plan
  - ✓ more robust non-financial performance measures
- Parliamentary oversight could be strengthened – must present timely audited accounts
- Effective monitoring only possible with political support
- Should be consequences if an SOE does not meet ROE target
- Does a holding company structure improve monitoring?

Legislation, Monitoring, Governance

SOE Performance Indicator	Fiji	Marshall islands	Samoa	Solomon Islands	Tonga	New Zealand
Legislation						
SOE Specific Legislation	YES		YES	YES		YES
CSO provisions and Guidelines	YES		YES		YES	
SOE Act implemented	YES				YES	YES
Monitoring						
Responsible Minister	YES		YES	YES	YES	YES
Ownership Monitor	YES		YES	YES	YES	YES
SOEs Operate Within Tight Budget Constraints					YES	YES
Requirement for SCI or business Plan	Yes		YES	YES	YES	YES
Profitability Target Set (such as ROE)	Yes		YES		YES	
Governance						
Skills based Appointment Process for Directors operating					YES	YES
Politicians and Civil Servants not appointed as SOE Directors						YES
Good Governance Principles enforced	Yes				YES	YES
Evidence of Political Commitment to Reform					YES	
Average ROE	0.70%	-13.20%	0.20%	-13.90%	6.00%	5.09%

Common Myths: 1 to 3

- *SOEs should not provide a commercial return; they should instead focus on delivering essential services to the people*
  - ✓ *The commercial mandate of SOEs is fully compatible with their community service obligation and provides incentives for efficient service delivery*
- *Only SOEs can fulfill CSOs; if SOEs are commercialized or privatized, CSOs will be discontinued*
  - ✓ All CSOs should be provided on a commercial basis so that the government can seek the most efficient providers
- *Commercialization is not delivering results*
  - ✓ *Those SOEs that continue to perform poorly post-corporatization have not completed the commercialization process*

Common Myths: 4 to 6

- *SOEs are vital generators of employment*
  - ✓ SOEs actually employ a relatively small proportion of the formal workforce, and if sold they would still employ staff
  - ✓ SOEs crowd out the private sector and therefore depress the rate of job growth
- *Privatization results in increased tariffs*
  - ✓ There is significant evidence demonstrating that the private sector is a more efficient provider of public services than the public sector
  - ✓ Tariff increases occur when subsidies are reduced and/or service quality improves with investment, not when delivery shifts from public to private sector
- *Public Servants play a vital role on SOE boards*
  - ✓ While they can bring knowledge and skills, they also bring conflicts of interest; time constraints; and adverse legal consequences

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Common Myths: 6 to 9

- *There is insufficient depth in the private sector to populate SOE boards*
  - ✓ Training, judicious use of ex-pats and business mentors is helping to address this
- *Only profitable SOEs can be successfully privatized*
  - ✓ Little value is added through pre-privatization restructuring: the buyer is best able to identify future value-adding strategies
  - ✓ Successful privatization of SBC and Tonga Machinery Pool demonstrate that unprofitable SOEs can be sold successfully w/o pre-sale restructuring
- *SOEs are needed to solve market failures*
  - ✓ In most cases the Government can address market failure through enhanced regulation and the introduction of policies that encourage private sector investment; the creation of SOEs is often the least efficient or effective solution

Recommendations

- Fiji:
  - ✓ Develop and implement SOE restructuring plans
  - ✓ Update SOE and Companies Act
  - ✓ Discontinue practice of appointing public servants to SOE boards as directors and monitoring staff as observers
- Marshall Islands:
  - ✓ Adopt an SOE policy and enact SOE Act
  - ✓ Establish an ownership monitor and a Responsible Minister for the SOEs

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Recommendations (2)

- Solomon Islands:
  - ✓ Train SOE directors on the implications of the new SOE law
  - ✓ Fully implement the Act and Regulations
- Tonga:
  - ✓ Continue to rationalize the SOEs
  - ✓ Increase the level of contracting out in the monopoly infrastructure SOEs
  - ✓ Objectively assess the merits of establishing an SOE holding company
- Samoa:
  - ✓ Fully implement SOE Act and Regulations
  - ✓ Update SOE Ownership and Divestiture Policy