

TECHNICAL ASSISTANCE COMPLETION REPORT

Division: SAPF

TA No., Country and Name: TA 4879 – MLD: Restructuring and Privatization of State-Owned Enterprises		Amount Approved: \$400,000	
		Revised Amount: \$400,000	
Executing Agency: Ministry of Finance and Treasury (MOFT)	Source of Funding: Technical Assistance Special Fund (TASF)	Amount Undisbursed: \$29,294.00	Amount Utilized: \$370,706.00
TA Approval Date: 01 Dec 2006	TA Signing Date: 06 Mar 2007	Fielding of First Consultants: October 2007	TA Completion Date Original: 31 Jan 2008 Actual: 30 Sep 2010
			Account Closing Date Original: 30 Dec 2010 Actual: 16 Nov 2011

Description

The Government of Maldives (referred herein as Government or GoM) requested the Asian Development Bank (ADB) to provide a technical assistance (TA) for preparing state-owned enterprises (SOEs) reform project to promote the private sector as a partner for national economic development. On 1 December 2006, the ADB approved a technical assistance (TA) in the amount of \$400,000 to the Government of Maldives (GoM) for the purpose of helping with the restructuring and privatization of SOEs. With a weakening economy, the performance of a number of SOEs have deteriorated over time and the Government had to provide financial support in the form of grants, subsidized loans and guarantees to ensure continuity of their operations. With the objective of reducing the public sector presence in the economy and mitigating pressures on fiscal budget, the GoM planned to reform underperforming SOEs by means of business mix optimization, workforce rationalization, financial restructuring and privatization.

The Ministry of Finance and Treasury (MOFT), the Executing Agency, identified: (i) 3 SOEs for privatization i.e. Maldives Industrial Fisheries Company Limited (MIFCO), Maldives National Shipping Limited (MNSL) and Public Works Services (PWS) (formerly, the Nasandhura Palace Hotel was identified and was later replaced with PWS); and (ii) State Electric Company Limited (STELCO) for restructuring. These SOEs were part of a pilot program to enable the GoM to build its capacity and gain experience and skills in implementing reforms of SOEs so that such reform can be extended in the future to the remaining enterprises not covered under the current program.

Expected Impact, Outcome and Outputs

The impacts of the TA were to improve the allocation of fiscal resources and stimulate private sector activities, and for the Government to initiate reforms of SOEs and to improve those enterprises' contributions to economic growth and social development. The expected TA outcome was to assist the Government in designing and implementing SOE reforms. As such, the outputs of the TA were as follows:

Output 1: Develop an institutional framework for planning and implementing SOE reforms through: (i) set up of organizational structure and empowerment mechanisms within the existing Public Enterprises Commission and Public Enterprises Monitoring and Evaluation Board (PEMEB), domiciled within the MOFT, as the central agency for implementing SOE reform measures; and (ii) identifying and advising the GoM on the regulatory framework needed to facilitate the implementation of those reform measures.

Output 2: Prepare business restructuring plan for STELCO while being retained under government ownership (after change of Government in late 2008 this policy changed to privatization plus decentralization of STELCO activities by regional island groupings) and with the objective of achieving sustainable financial viability. The assistance included: (i) identification of business restructuring measures; (ii) financial restructuring through either or combination of debt or/and capital; and (iii) organizational and workforce restructuring measures including overhaul of management and governance.

Output 3: Advise and assist the GoM in disinvesting its shareholdings in the 3 identified SOEs through public share flotation and/or bringing in strategic partner.

Output 4: Build the capacity, experience, and skills of the GoM in implementing SOE reforms that can be extended to the remaining SOEs.

Delivery of Inputs and Conduct of Activities

Given the scope of the TA within an implementation originally envisaged within an 8-month period and the challenging political situation in Maldives, the delivery of the inputs were significantly delayed and in part due to changes in the TA scope and implementation arrangements, including a contract variation and 3 extensions that took implementation period to over 2 years.

First, during short listing of consultants in February 2007, feedback was received from several firms and their price proposals were beyond the budget under the TA. Hence, the GoM requested for a minor change of scope, which was approved on 26 March 2007, in order to (i) revise the terms of reference, (ii) provide for four international individual consultants, and (iii) realign the budget allocating additional \$30,000 from the contingency resource. Due

to delays in recruitment, a request for an extension of the TA completion date was sought and approved from original date of 31 January 2008 to December 2008 to provide the consulting firm with ample opportunity to undertake the TA activities. An international consulting firm, Adam Smith International (ASI) with local partners FJS Consulting advised on the privatization of MNSL and PWS, and the restructuring of STELCO. Individual consultants (hired through a firm – Deloitte & Touche Consulting India Pvt Ltd.) advised on the other elements of the TA. Consultants were fielded in late 2007. Recruitment of all consultants under the TA was done in accordance with the *Guidelines on the Use of Consultants by ADB and its Borrowers*.

Second, a contract variation was requested following GoM's request for ASI to provide additional capacity assistance on the following: (i) day to day support to GoM in taking forward the MNSL and the STELCO privatization transactions; and (ii) preparation and presentation to the Cabinet of a formal privatization policy of SOEs with a clear statement of intentions; (iii) preparation of draft Cabinet orders on privatization including categorization framework of SOEs, guidelines for financial restructuring, and framing of a redundancy package. As such, an extension of the TA was sought and approved to 31 December 2009 to accommodate the changes in the scope of the TA.

Third, the activities of the consultants were put on hold in mid to late 2008 due to: (i) GoM's preparation for Maldives first democratic Presidential election; and (ii) the Parliament review of proposals on the privatization policy of SOE and the establishment of a holding company. Given that consultants' recommendations on SOE reform are dependent on the outcome of the Parliament adopting these proposals, consultancy work on restructuring and privatization could not proceed as planned. The latter issue was resolved only in mid-2009 and as a result, the final reports of the consultants could not be submitted before 31 December 2009. The Government sought another extension of the TA agreeing with ADB and the consultants that the final reports will be made available by 30 September 2010. Hence, ADB approved the final extension date of the TA.

By all accounts, the delivery of inputs and outputs produced by the consultants were satisfactory and is consistent with the performance evaluation and ratings provided by the ADB project officer involved with the implementation of the TA. Performance of the EA was partly satisfactory with changes in key staff within PEMEB (who is supporting the MOFT as the EA) and lack of communication among identified SOEs of the reform measures being undertaken by the Government, thereby affecting the timely delivery of the TA activities. ADB's performance was also satisfactory having worked closely with the Government to achieve resolutions to deliver the work programs under the TA despite challenging political conditions in Maldives. Key lessons can be drawn from this experience, as highlighted in this report below.

Evaluation of Outputs and Achievement of Outcome

All outputs of the TA were achieved and were of good quality. The MOFT expressed satisfaction with the delivery of the activities and submission by the consultants of their final reports and recommendations on: (i) organizational development of the nodal agency for SOEs Reforms in Maldives (submitted by Deloitte); (ii) restructuring issues and options for STELCO (submitted by ASI); (iii) strategy for private sector participation for MIFCO (submitted by Deloitte); (iv) options and issues for PWS (submitted by ASI); and (v) privatization issues and options for MNSL, including preparation of various due diligence reports, draft bid documents and tender procedures, and draft sale and purchase agreement (submitted by ASI). Completion of the TA was significantly delayed, however, due to the changes and additions in the activities explained in the previous section. Based on review of project documents, reports and views gathered from the consultants, the achievement of outcomes which depended on the implementation by the GoM of the consultants' recommendations for SOE reforms proved challenging due to a number of factors, including but not limited to:

(i) **Lack of communication by GoM of its intention to privatize/restructure identified SOEs**, It appeared that key officials of SOEs (particularly from MIFCO) had not been aware of the privatization that was being contemplated by the government, and was not involved in preparing the TOR. Consequently, officials were not prepared with relevant information required for the assessment resulting in considerable delays in sourcing information and data relating to entity's operations and financials.

(ii) **The frequent changes and staff reassignments in the MOFT / PEMEB**. PEMEB is a relatively small organization and is limited to one or two key individuals. The changes and reassignment of key staff led to an absence of a full time head or identified coordinator who could ensure requisite participation from various agencies/ individuals within the government, and the timely provision of counterpart inputs, comments on deliverables etc.

(iii) **The facts and circumstances of the enterprises were found to be substantially different as time went by.**

(a) MNSL financial performance worsened dramatically during the course of the project and became insolvent. A full bid process was implemented and after evaluation of offers it was decided that an orderly winding up of MNSL rather than a sale on unfavorable terms with continuing huge financial exposure into the future for GoM was the best outcome in the circumstances.

(b) STELCO changed from being restructuring to privatization after the change of Government. STELCO began to enter negotiations and an agreement with an unsolicited bidder for renewable energy projects, the Government wished to operate regional entities to provide infrastructure facilities and services / utilities so these were major changes in direction during the project.

(c) PWS, on the other hand, was found not to be suited to privatization and of no interest to private sector operators. It was an unincorporated unit that depended for 70% or more of its work on Government contracts.

GoM decided to merge it with Male Municipality.

Nevertheless, it should be noted that the TA provided the GoM with the required tools and processes needed to take further SOE reforms going forward. The due diligence investigations, the criteria for deciding on SOE reform options, the privatization procedures produced for MNSL, the tender documents, the information memorandum and draft agreements, the evaluation of bids all served to build up knowledge and experience in GoM on how to apply best practice SOE reforms and privatization practices and procedures. A privatization policy document and other documents supplied to the privatization committee towards the end of the project provide a solid basis for implementing SOE management and reform including privatization in Maldives.

Overall Assessment and Rating

The TA is rated as successful given that the outcomes were substantially met in terms of (i) providing an organization framework for PEMEB and Privatization Commission, and (ii) developing restructuring/ privatization plans for MIFCO, STELCO, and MNSL, as well as PWS closure. In the case of MIFCO, prior to full privatization, restructuring was needed and subsequently implemented to ensure successful privatization by attracting reputed strategic partners from the market. STELCO was also restructured into several independent entities for which a roadmap for privatization was also developed. On the other hand, MNSL was put up for privatization but no viable bid was received. To have sold it on the poor terms would have exposed GoM to greater losses than an orderly winding up.

Despite consolidated efforts from the ADB and consultants, the GoM has not been able to implement the recommendations at that time, as a result of the: (i) lack of political will to implement such reforms; (ii) the general lack of interest from the market; and (iii) the Parliament now placing heavy requirements on future privatizations by passing a controversial amendment to the Public Finance Act declaring that the Government can only lease a state asset or borrow money from a foreign donor under specific legislation approved by the Parliament.

Nevertheless, the reforms initiated under the TA were taken as part of policy matrices under the ongoing ADB Economic Recovery Program (ERP)¹ towards future privatization of several SOEs in order to promote private sector development in Maldives. Hence, part of the tranche release condition under ERP is for the privatization committee of the GoM to bring to the point of sale (i.e. completion of all the steps leading to the bid out stage) of 3 identified SOEs – as follows:

- (i) A share issue privatization of Dhiraagu (a telecom company) was successfully implemented with the sale of 7% share by the Government to the Cable and Wireless Communications;
- (ii) A management contract was awarded through competitive bidding process for the rehabilitation, expansion, modernization, operation and maintenance in relation to Male's international airport in June 2010 to a private sector consortium, GMR-MAHB; and
- (iii) An asset sale privatization of MNSL. As previously indicated, the Government decided to dissolve the company given deteriorating financial condition of the firm.

Major Lessons

It is important that in order to ensure the achievement of intended outcomes, extensive stakeholder consultations should be held during the preparation of the TAs so that all concerned organizations / agencies / beneficiaries are aware of the rationale and objective of the initiative being undertaken and that key officials are on board. Whilst proving difficult in many of ADB's DMCs to retain government / counterpart staff during project implementation without civil service reforms (i.e. improvements or reforms in the methods of appointment, rules of conduct, etc. that affect the organization, performance and working conditions of civil servants or government employees), it is important that ADB should actively engage with the EA to ensure succession planning to avoid significant delays during implementation, and to the extent possible ensure that the counterpart staff remains in the position for the duration of the project. Moreover, in designing the scope of the TA, it should look carefully at implementation risks and anticipate action plans to mitigate those which include structuring TAs in a manner that disbursements are linked to achievement of milestones or outcomes or can be followed through in any of ADB's ongoing complementary work program in a country to achieve sustainability of desired outcomes. In this case, the continuity of these reforms under the TA was subsequently taken as part of policy matrices under the ERP to promote privatization of SOEs so as to improve the soundness of GoM's fiscal resources and stimulate private sector activities in Maldives.

Recommendations and Follow-Up Actions

Based on the lessons of the TA: (i) it is highly desirable that the MOFT should actively pursue its SOE reforms policy to promote private sector development; and (ii) it is necessary to continuously monitor the progress of the policy actions under the ERP in order to complement the work achieved under the TA.

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¹ ADB. 2009. *Report and Recommendation of the President to the Board of Directors on the Proposed Program Loan, Technical Assistance Loan, and Technical Assistance Grant to the Maldives for the Economic Recovery Program*. Manila.