# The Strategy and Governance of SOEs in Africa: Lessons Learnt and Policy Implications

**Arkebe Oqubay**

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DSI/NRF SOUTH AFRICAN RESEARCH CHAIR IN INDUSTRIAL DEVELOPMENT

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## Abstract

A widely held view is that state-owned enterprises (SOEs) are disastrous for economic development on conceptual and empirical grounds. And indeed, there are prominent examples that confirm how bad they are. However, this paper attempts to turn some of this on its head and argues that, despite obvious evidence that many SOEs are awful, there are good reasons and sound evidence to support a very different argument. With a focus on the challenges and lessons of the governance of SOEs in Africa, this paper argues, first and foremost, that ownership *per se* does not tie up firmly with corporate performance as much as universally supposed. But more than this, SOEs are at the heart of transformation and economic catch-up, as they have been in many places – a perspective underpinned by the developmental role of the state in accelerating capitalist development. SOEs are playing increasingly prominent roles worldwide in the early twenty-first century. Second, developing productive and high-performance SOEs requires a more disciplined state that promotes the constructive political condition for the productive role of SOEs, restrains harmful political interventions, and articulates the public policy purpose of the SOEs. Third, a vibrant SOE sector necessitates enhancing the governance system – both the supervision and administration of SOEs – and developing corporate governance within each SOE that constantly evolves with the best international experiences. Fourth, firms' performance requires a complex and painstaking effort to build capabilities and strategies specific to the industry in an increasingly intense international competitive force. However, this undertaking is more complex than often thought, and the governance of SOEs and a disciplined state are necessary, but inadequate. This paper presents empirical evidence, draws lessons from across the continent, and combines these with learning from international experience. It builds on a qualitative and comparative research approach, utilising a mix of document reviews and selected qualitative interviews, with a particular focus on policy lessons. SOEs are dominant players in South African and Ethiopian economies, and are suitable cases from which to extract policy lessons.

**Keywords:** SOEs, government, industrial policy, economic transformation, corporate governance, Africa, firm capability

**JEL codes:** H4; H7, H8; L2; L3; L5; O1; O2; O3; P4

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## List of Abbreviations

| | |
|---|---|
| ANC | African National Congress |
| CBE | Commercial Bank of Ethiopia |
| CEO | Chief executive officer |
| DBE | Development Bank of Ethiopia |
| EAL | Ethiopian Airlines |
| EELPA | Ethiopian Electric Power Authority |
| EEP | Ethiopian Electric Power |
| EEPCO | Ethiopian Electric Power Corporation |
| EEU | Ethiopian Electric Utility |
| EPRDF | Ethiopian People's Revolutionary Democratic Front |
| FDRE | Federal Democratic Republic of Ethiopia |
| IDC | Industrial Development Corporation |
| IMF | International Monetary Fund |
| METEC | Metal and Engineering Corporation |
| OCP | OCP Group (Office Cherifient des Phosphates) |
| OECD | Organisation for Economic Co-operation and Development |
| SAA | South African Airways |
| SADB | South African Development Bank |
| SASAC | State-owned Assets Supervision and Administration Commission of the State Council |
| SOE | State-owned enterprise |
| SGCC | State Grid Corporation of China |
| WB | The World Bank Group |

# PART I: FRAMEWORK AND CONTEXT

## 1. Introduction

Why do SOEs matter, and what is the rationale for their role in economic development? Does ownership matter for firm performance? What are the challenges of and lessons from building a vibrant SOE sector? These are strategic issues that concern policymakers and require pragmatic responses rather than dogmatic prescriptions. SOEs administer an enormous public resource, with significant economic growth and accountability implications. Over 1 000 national-level SOEs in Africa are deploying about US$ 1 trillion in assets, accounting for 5% to 35% of the GDP of national economies, and employing nearly 1.5 million people across sectors in 2020. Worldwide, the role of SOEs increased in the 2010s, particularly in emerging and developing economies, and hey currently account for US$45 trillion worth of assets and for 20% of the world's largest Fortune 2000 corporations.[1] SOEs have increasingly expanded operations internationally since the 2010s.[2]

However, significant heterogeneity across African SOEs is shaped by historical factors, national contexts, ownership structure and firm size, sector features, and government policies. The performance of SEOs has been mixed, and empirical evidence suggests that SOEs have lower financial performance in terms of aspects such as profitability and revenues. Nonetheless, this evidence does not acknowledge the conflicting policy goals obligated on SOEs, and the political environment in which they operate. The mixed and inadequate performance of the SOE sector, and the limited outcomes of reforms, have brought the agenda to the forefront. In some cases, the crisis in giant SOEs in public utilities has become a dominant political concern. The "state capture" report of systemic corruption in SOEs has magnified the vulnerability of the SOEs' governance system and the risks of "political" intervention.[3] Hence, the necessity of SOEs in African economic transformation, and the underperformance and political risks, put significant pressure on governments to address this fundamental concern.

Historically, state-owned or public enterprises are familiar and have existed for over a century in Africa, and even much longer in developed economies such as Europe.[4] Both OECD countries and emerging economies have used SOEs to pursue public policy and commercial purposes. Unlike the conventional assertion on economic liberalisation and privatisation, and

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[1] International Monetary Fund ([IMF] 2021a, 2021b).
[2] The world's most prominent development banks are state-owned: China Development Bank, Brazil's BUNDES, and the multilateral World Bank. In terms of asset capitalisation, the most valuable is ARAMCO, estimated at over US$ 1 trillion. China's State Grid is the world's largest electricity utility provider, serving over 1.1 billion commercial and household customers. Singapore has the highest concentration of SOEs and is among the high performers worldwide. See Kanyane & Sambo (2021) on BRICS.
[3] See Zondo Commission Enquiry https://www.statecapture.org.za/
[4] A notable example is the East India Company, partially owned by the British state, which became one the most powerful corporations worldwide. It was founded in 1600 as a joint stock, controlled world trade, and had its own army and vessels.

experiences in late industrialising economies, SOEs can play a strategic and developmental role in driving industrial transformation and economic catch-up, as witnessed in East Asian economies.[5]

A comparative research approach supported by multiple cases was used for this study. Ethiopia and South Africa stand among African countries with a long tradition of SOEs in diverse sectors. Considering the availability of data and the author's access, Ethiopia and South Africa were used as national case studies because their SOEs have a century-long legacy, have been through diverse political systems, and have been involved in multiple sectors. A few sectors were selected as case studies. The paper's methodology draws from extensive document reviews and official records of the SOEs or relevant government bodies. It also uses an observer-participant method to benefit from the author's experience.[6] Moreover, qualitative interviews and consultations with appropriate experts and board members were conducted.[7]

The paper has six sections. Following the introduction, Section 2 presents the analytical framework and mapping of African SOEs to provide the context. Section 3 reviews the performance of SOEs in the energy sector in Ethiopia and South Africa. Section 4 focuses on reviewing the SOEs in the aviation industry to extract lessons. Section 5 focuses on SOEs in the telecommunications, logistics and banking industries. Section 6 presents the comparative insights and synthesis of SEOs in development, focusing on developmental roles and an effective governance framework. The final chapter presents a strategic approach to reforming SOEs and pathways to the future.

## 2. Analytical Framework and Mapping of African SOEs

### 2.1 Mapping African SOEs

There were over 1 000 state-owned enterprises operating in Africa in 2022, according to data compiled from national and international sources.[8] They employ over one million workers,

[5] Amsden (1989, 2001); Gerschenkron (1962); Hirschman (1958, 1968), Mkandawire (2001); Lee (2019); Mazzucato (2013); Wade (2004); Zenawi (2012).

[6] The author has served as a policymaker, sitting on various boards of leading public enterprises, and as a Senior Minister and Special Adviser to the Prime Minister of Ethiopia coordinating economic sectors.

[7] UNECA (2021a, 2021b) conducted a commendable study in collaboration with South Africa's Department of Public Enterprises and Wits University on SOEs in South Africa and other Southern African countries. A high-level policy dialogue in Johannesburg concluded this initiative in July 2022 in the presence of Minister Pravin Gordhan.

[8] There is a lack of reliable data on African SOEs for various reasons, including the vague definition of controlling share of ownership in these enterprises, some enterprises operating sub-nationally (such as water utilities), and the lack of a database or portal continuously updated at the country and continent levels. An additional source of confusion is that entities such as broadcasting corporations, park administration, or agencies with regulatory power (like civil aviation), and entities with autonomy and considered statutory boards (such as investment or economic boards), are often merged as SOEs. There is a need for a central agency that provides reliable and

primarily modest-paying jobs, and in many African countries they account for 5% to 20% of the GDP and 30% to 50% of exports. However, these SOEs exhibit significant heterogeneity in sectoral distribution, size and capability, and their policy impact and commercial performance show mixed outcomes. SOEs have existed in many African countries since they gained political independence, and they predate the nineteenth and early twentieth centuries.[9] With significant changes in ruling regimes, SOEs have witnessed both discontinuity changes and continuity regarding their mission, ownership, and roles. This paper focuses on SOEs operating in economic sectors but excluding sovereign wealth fund administering agencies, whose data is not public.[10]

Despite the presence of SOEs in most African countries, there is immense variation on the distribution and roles due to disparities in policy directions and historical background. For example, SOEs are highly concentrated in fewer countries, such as Egypt, Ethiopia, and South Africa.[11] For instance, South Africa had over 700 SOEs administered by central, provincial and local government agencies in 2020. Eskom is Africa's largest energy utility operator, accounting for two-fifths of the electricity supply. South Africa is also home to the most prominent development banks in Africa, including the Development Bank of Southern Africa (DBSA) and the Industrial Development Corporation (IDC). In the mining industry, the OCP Group, Morocco's largest SOE, was founded in 1920 to mine and export phosphates and chemicals. Ethiopian Airlines, Africa's largest carrier, is the country's most significant contributor to services export and functions as the government's policy arm.

Furthermore, the roles and mission of SOEs have changed over time, caused by the demands of the stage of economic development and changes in the political system. South African SOEs have repurposed their vision and mission to reflect the end of the apartheid regime and the post-1994 democratic political system led by the ANC. In Ethiopia, leading SOEs were founded under Imperial rule and increased under the command economy of the Derg military regime (1975 to 1991), and rationalised to strategic public enterprises after the 1991 democratic transition.[12] This illustrates that SOEs have to redefine their purpose to achieve the economic

comprehensive data on SOEs, and there is much diversity in the legislative framework and corporate governance of SOEs.

[9] South Africa's Eskom was founded in 1923, SAA in 1934, and the IDC in 1940. Ethio-Telecom was founded in 1894, Ethiopian Airlines in 1945, and Morocco's OCP in 1920. Many railway companies, such as Egyptian, Nigerian, and Ethio-Djibouti, are over 100 years old and have undergone significant restructuring of organisation and ownership.

[10] SOEs considered as the focus of this research are those economic entities established by government legislation as commercial entities that should follow the country's commercial law applicable across all commercial entities.

[11] For a comprehensive review of Ethiopian and South African economies, see Andreoni et al. (2021); Cheru et al. (2019); Oqubay (2015); and Oqubay et al. (2021).

[12] The list includes the Commercial Bank of Ethiopia, Ethiopian Airlines, Ethio-Telecom, and electricity utility companies.

policy of their respective governments, and governments have to deal with the issues of legacies.

However, in many African countries the SOEs continue without repurposing and transforming themselves to the development strategy and government policy. Almost all African countries have experienced a change in ownership and privatisation. Nevertheless, the motive and policy driving ownership differ among African countries and industries – from rationalising assets and reorienting policy to implementing economic liberalisation prescribed by the Washington Consensus. Another critical feature in the scope and depth of utilising SOEs in the economy is the sectoral diversity and multiple roles they play across various industries, including in development financing, primarily to boost productive capacity, infrastructure development and utilities, and serving in the wealth management of national endowments. This is typical in extractive industries (mineral resources), and the oil and gas sectors, and not necessarily as a driver of industrial policy.[13]

Three significant factors characterise the context of African SOEs. First, historical legacy plays a critical role, as shown in the following sections of the paper. Many SOEs that were established decades ago were likely to continue, despite the change of government. In the case of Ethiopia, this was from Imperial rule in the early twentieth century to the military regime and current regime, and in South Africa they transcended the apartheid regime and the post-apartheid democratic regime. Some of these SOEs were only founded because they were transferred from previous governments. Second, deploying SOEs has been connected to the particular endowments of the respective African countries. Most of the established SOEs are in mineral and extractive industries and oil and gas sectors. Typical examples are the OCP of Morocco and Angola. Countries with ports and related infrastructure are commonly those that have coastal access and lie in transhipment routes. Third, the national government's political orientation, aspirations, and development paths are the key drivers of pursuing SOEs, nationalisation, or privatising public enterprises. A global context that is conducive to the planned economy or role of states has a broader influence, as the 1960s and 1970s were conducive to the state's role, followed by the 1980s to 1990s, with privatisation and economic liberalisation becoming dominant, and the 2000s to 2010s, when the state's role was acknowledged in coping with the global financial crisis in 2009.[14]

### *2.1.1 Why SOEs matter, and the imperative for SOEs*

Various terms are used to refer to state-owned enterprises (SOEs), including state-owned companies (SOCs), public enterprises, and government-linked companies (GLCs). Broadly defined, SOEs are companies wholly or partly owned and controlled by the government, with

[13] Kokil (2022); Limbo (2019); Mbo (2017); Ministry of Finance of Zambia (2022); Ministry of Public Enterprises, Namibia (2022); National Planning Commission ([NPC], 2019).
[14] See Ismail (2018).

policy goals but operating under the country's commercial law. SOEs are distinct from non-commercial government entities such as agencies or statutory boards. Two marked features of SOEs are that these entities are owned by the state and constituted as commercial entities per the country's commercial or corporate law.

Empirical evidence suggests that African SOEs have the potential (prospect) to drive transformation and economic catch-up, playing specific roles to serve the state's development strategy. The extent and type of role evolves with the level of economic development and diverges across sectors and the particular context – capacity of the private sector and political landscape favouring public investment. The roles of SOEs can be classified into four categories:

*Inducing investment*: SOEs play a role as industrial policy instruments to generate investment through two channels. This first is making a direct investment for demonstration effect or filling the gap in industrial capacity as a primary mechanism, and ownership may change gradually to private hands.[15] A second channel is providing development finance to industrial actors to stimulate investment in key priority sectors or firms aligned with the government's industrial policy. Development banks have been considered flagships of developmental states and conduits of subsidised loans for industrialists.[16] Governments build these SOEs as 'national champions' (or global champions) operating within domestic and international markets.[17]

*Natural resources*: Governments establish SOEs to administer natural resources (such as mining resources and gas and oil) as national sovereign wealth instated in the country's constitution and to maximise the commercial return on the asset. Examples are Morocco's OCP and the Saudi ORAMCO or Norway's Statoil.[18]

*Natural monopolies in public utilities*: Governments apply SOEs to cope with the complexity of dealing with natural monopolies, such as electricity transformation and distribution networks, where competition and market laws are constrained. Power utilities and public transport are examples. In most cases, consumer bills are highly regulated by the government.

*Stimulate innovation and technological capability*: Governments may also establish SOEs to stimulate innovations in frontier technologies in which scientific breakthroughs are required, and socialising risks and managing uncertainty are vital. This can be done in diverse ways,

[15] South Korea's POSCO is a notable example (Chang, 1994).

[16] See Di John (2020); Griffith-Jones and Ocampo (2018); and Woo (1991).

[17] See Nolan (2014); Li and Chen (2020). National champions could be SOEs in China or private industrial conglomerates like the South Korean Chaebols. China has been pursuing developing about 100 national champions, administered under the central government's Supervisory Agency of State Assets of China (SASAC)

[18] See Norwegian Ministry of Trade, Industry and Fisheries (2020), OECD (2015c, 2016, 2021b). See also Musacchio & Lazzarini (2014) on state capitalism and SOEs.

depending on the scope and direction of technological development, such as space technology, the defence industry, and new chip technologies.[19]

### *2.1.2 Disciplining the state and building productive SOEs*

A developmental perspective views the state's developmental role positively, which is essential for driving structural transformation and catch-up. It further views the state as playing an active role in structural change and economic catch-up, and that the state and market co-exist, playing complementary roles. The relative positions of the state diverge across sectors and over time.[20] The specific role of SOEs emanates from the state's developmental role in pursuing industrial and public policies. However, developing high-performance SOEs is more complex than ordinarily assumed, and various factors play beyond policy design and political commitment. First and foremost, the state must examine SOEs' rationale and productive role, given their grand mission and development strategy. The state should understand that developing a productive SOE sector requires a disciplined government that provides strategic and political direction, while insulating the sector from harmful political intervention. This necessitates a comprehensive, well-articulated SOE policy and governance framework, and regular reviews.

Second, it called for managing conflicts within the state's multiple roles – as an owner of the SOEs, a regulator (of broader competition practices and sector-specific regulations), focal sectoral public policy, and a major purchaser through public procurement. The basis for managing the conflict has to be based on the principles specified in the Constitution and related laws, which is a critical facet of a disciplined state. The owner role is the basis for governance systems of SOEs, including financial goals, the autonomy and independence of SOEs, and the independence of SOEs and synergies. Third, defining the purpose of the specific SOE is the basis for reducing the tension and conflicts within the dual goals: public policy and commercial objectives. The purpose of the existence of the SOE is critical for the continuous alignment of the strategic roles in line with the sector's features and level of development. A constant review would examine whether private players can substitute, enabling the state to focus on new frontiers and strategic goals. This exercise ensures that the SOE continues to thrive and effectively implements the government's industrial policy.

[19] See Chang (1994); Mazzucato (2013).

[20] The roles of SOEs and their governance are viewed fundamentally from Marxist, mainstream economics and heterodox perspectives. The primary economic direction is a Marxist view that the state is an apparatus necessary for exercising proletarian dictatorship and nationalising the means of production to serve the masses and build a socialist economy. Mainstream economics, particularly the neo-classical, views resource allocation as being left to market forces, and that state intervention should be limited to market failures. Neoliberalism, symbolised by the Washington Consensus, puts economic liberalisation and privatisation forward as the recipe, underlining that the state's roles should be narrowed.

Furthermore, the governance of African SOEs entails two aspects – the governance of the SOE sector as a whole, which should be consistent with the state's laws and principles of economic governance, and the corporate governance within SOEs, ensuring that enterprises adhere to the government laws enacted for SOEs and operate within the commercial code and conventional practices of the corporate realm and critical sectoral competitive requisites. On both levels, empirical evidence suggests that the existing policies and practices in many African countries are diverse and have massive potential for improvement. Specific governance matters that have significant influence and shape SOEs' performance include the selection of the board of directors and the appointment of executive management, the relationship between the SOEs and the supervisory agency and sectoral regulatory body, managing the inherent tension between public policy and commercial goals and, like all commercial entities, managing the inbuilt owner-agent conflict. A well-functioning governance system should ensure high performance and achieve the SOE's purpose, meeting public resources' highest level of transparency and accountability while constantly adapting to new realities. Building a vibrant and accountable SOE sector is challenging and a double-edged sword.

## 2.2 Analytical Framework

This paper draws perspectives from structuralist development economics, primarily on late development and the developmental state's roles, and industrial policy as an analytical framework, such as Amsden's contribution. Catch-up and latecomer industrialisation do not follow a linear development path and build on latecomer advantages, necessitating an active role for the state to play a developmental and transformative role through the pursuit of industrial policy to accelerate productive transformation and develop technological capability.[21] Nonetheless, the role of developmental states is neither uniform across industries nor through time. Amsden argues that developmental states should apply the reciprocity principle ("reciprocal control mechanism"), providing productive rents or "intermediate assets" to targeted firms tied to performance – both SOEs and private firms – and developing their capability. Amsden adds the vital role of development banks as the "flagship" of the developmental state in latecomer development, and emphasises the primary function of firm capabilities, strategies and building "competitive assets".[22]

The emphasis was on 'national leaders', nationally owned and controlled firms, which combine their 'competitive base' (domestic market) and globalising in international markets through exports and outward foreign direct investment. Amsden's notion of 'national leaders' is similar to 'national champions', widely used to refer to the SOEs in China or Chaebols in

[21] See Amsden (1989, 1997, 2001); Chang and Singh (1997); Andreoni and Chang (2019); Cherif and Hasanov (2019); Oqubay et al. (2020).

[22] See Penrose's theory of the firm and Chandler's work on the scale and scope and rise of large corporations (Penrose 1959; Chandler et al., 1997; Chandler 2004).

Korea. National champions and firm capabilities are equally related to SOEs or private firms, and the type of ownership is not considered an essential feature. South Korea's POSCO and many European SOEs or Chinese national champions are examples of productive SOEs.[23] From an industrial policy perspective, the state must develop targeted and selected SOEs with explicitly defined purposes. The government's industrial policy determines "national champions" in strategic priority industries and builds SOEs from a longer-term perspective to transform and be relevant to the stage of development.

Furthermore, there is no inherent contradiction or conflict between industrial policy and commercial objectives. Commercial objectives are not solely about profitability, but rather about comprehensive operational performance and sustained competitiveness, maximising long-term return on assets and economic sustainability. Indicators that focus on pure profitability would lead to short-termism rather than building strategic competitiveness. SOEs are also expected to be guided by stakeholder values rather than merely by shareholders. These implications emanate from the state ownership and primacy of industrial policy goals.

#### 2.2.1 Governance requirements

An industrial policy framework, however, needs to be revised regularly to review the contribution and performance of SOEs, putting the political conditions on the roles of government and requirements on firms. The governance of SOEs comprises two distinct dimensions: the governance of all SOEs, which involves political choices, and the internal corporate governance of SOEs, which is informed by international practices and national laws. Governing SOEs or managing the SOE sector focuses on improving the system between the government and the specific SOEs and the SOE sector, which varies across national experiences due to the particular political context of the government system and the level of economic development. It is influenced by lessons learnt from international experience. Ensuring that SOEs meet the government's policy and commercial goals, their performance and global competitiveness are developed, growth strategies are pursued, and reforming SOEs becomes a constant mission. Ensuring government officials and bodies respect government policy and legislation on SOEs is vital to ensure that the performance of the SOE sector matches the industry's benchmark and that sound governance systems are adhered to.

Managing the conflict between the government's roles as *owner*, *policy leader*, and *regulator* is an ongoing task of the government through various mechanisms such as the ministry, the council of ministers, and the parliamentary sub-committees. Regularly publishing annual reports on the state, performance and corporate governance of SOEs to the public, and periodic reviews by the cabinet and parliament, could improve transparency and

[23] See Li and Chen (2020); Lin (2021); and SASAC (2023).

accountability. Selected and purposeful learning from other international best practices would contribute to better governance systems.

### 2.2.2 Firm capability and 'competitive assets.'

Although state-owned enterprises are an instrument of industrial policy and developmental states, they are essentially firms or corporate entities operating under government laws. They must compete in a competitive market economy. Business management and industrial economics disciplines provide rich knowledge on the nature of competitive forces surrounding modern corporations. Drucker highlights the importance of corporate vision, purpose and mission. Porter underscores the role of corporate strategy and competitive pressures. Mayer argues that corporations must ensure 'stakeholder value', which underlies the firms' purpose and the multiple roles (as employer, investor, producer, supplier), rather than follow 'maximising shareholder profit' value that stands by short-term profits at the cost of all other stakeholders and long-term strategies. This is the main view of 'shareholder capitalism,' a dominant feature of the Anglo-Saxon corporate world. Chandler's pioneering notion of 'structure follows strategy' and Mintzberg's (1992) concept of the diverse features of organisational structure aligned to chosen strategies. In a constantly changing external environment and constant shifts in competitive forces, firms can only survive and grow if they are 'learning organisations' with the ability to adapt and transform themselves.[24]

Amsden (1997:469) furthermore emphasises that the focus on building firm competitiveness in late industrialisation is targeting domestic firms to become "professionally managed, large-scale modern corporations" in mid-technology industries and focusing on "pure learning", borrowing technology in commercialised products of foreign firms. Amsden (1997:469) argues that the "differences in mode of competition are wide-ranging, and include the structure of the business enterprise, the nature of learning and the role of the states", along with firm-specific technological capabilities to produce tradable goods for any market (namely, export markets). Amsden (1997:474) highlights that, in determining whether government policies generate economic expansion, "one must examine state strategy (or lack thereof) toward the development of *specific industries and firms*. For it is the success or failure of such ventures that ultimately determines the financial soundness of the state."

Innovation capability has been emphasised in an era of accelerated technological changes. Technological learning occurs in firms and demands absorptive capacity – the ability to recognise, assimilate, and apply new information.[25] Acquiring further information requires prior knowledge, and innovation requires borrowing from others. Learning by doing is critical to internalise new knowledge, but constantly improving productivity and firms with in-house R&D are more likely to internalise further information faster. Evidence from development

[24] See Chandler (1969); Porter (1985); Senge (1990); Mintberg (1992); Drucker (1993); Mayer (2013).
[25] See Oqubay and Ohno (2019); Cohen and Levinthal (1990)

economics, industrial economics, and business management provide rich literature that firm capability is built over a long period and requires the effective design and implementation of firm strategies. Amsden also highlights the importance of learning as the prime pathway to economic catch-up for both firms and policymaking. Amsden (1989:172) posits that the technological capability of late developers includes production capability (production management, production engineering), investment capability (workforce training, pre-investment feasibility studies, project execution), and innovation capability (in basic research, applied research, and development).

# PART II: EMPIRICAL EVIDENCE ON STATE-OWNED ENTERPRISES

## 3. Energy Sector: A Case of How an SOE can Hurt an Economy

Several African countries have SOEs in the energy sector along with electricity companies. Access to electricity and its affordability for low-income users makes it politically sensitive and it cannot be left to profit-driven operators. South Africa's Eskom and Ethiopia's EEPCO illustrate the challenges and dilemmas of government in developing the electricity sector and building capable corporations.

### 3.1 Eskom and the power sector

The Eskom case is a typical example of an SOE crisis that spiralled into a national debacle and weakened an economy. On 16 February 2023, President Cyril Ramaphosa announced the appointment of a Minister of Electricity, with the full responsibility to oversee all aspects of responses to the electricity crisis as a matter of utmost urgency, which gave high expectations of ending the blackouts.[26] However, the critical question is whether it will effectively contribute to solving the crisis, or whether such change is a cosmetic one that only adds complications to the existing structure, namely the existing supervisory agency, the Department of Public Enterprise, and the energy policy arm, the Department of Energy and Mineral Resources. Does it help to address the root cause of the crisis?[27]

With its origins in the 1920s, Eskom is Africa's largest electricity utility provider, accounting for 45 GW of generation capacity. It is also the biggest SOE in South Africa, with an approximate asset of ZAR 1 trillion. Its track record includes that it was among the leading electricity utility companies. As reported by the Zondo Commission, Eskom was among the

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[26] https://www.gov.za/news/speeches/president-cyril-ramaphosa-replies-questions-national-assembly-11-may-2023

[27] Eskom's grave situation was not reversed, and on 9 October 2023 the Board Chair resigned, and the CEO post has remained vacant for over eight months. The new structure is further complicated given that Eskom's board represents the owner and provides strategic leadership, further diluting accountability given the legitimate mandates of the Department of Public Enterprises and the Department of Mineral Resources.

SOEs that became a ripe ground for state capture.[28] Political intervention and conflicting interests of corporate governance have dominated the public discourse on Eskom. Furthermore, the Eskom case illustrates the fundamental issues that led it from being Africa's most efficient operator in the 1990s into a crisis that has made it a "too big to fail" dilemma.

Eskom carries a heavy stake in South Africa's economic trajectory. First, energy is vital to accelerating economic growth and narrowing inequalities in South Africa by expanding industrial capacity, attracting new investment, supporting small businesses. Most importantly, the electricity crisis primarily constrains employment creation.[29] Access to utilities and service delivery are interlinked with affordable electricity supply. Second, South Africa's green transition and decarbonisation are urgent and central to South Africa's transformation, which depends on Eskom. Third, given Eskom's heavy indebtedness, the delay in reversing the crisis has affected creditors and the government, which acted as a loan guarantor. Finally, the ruling party's legitimacy depends mainly on addressing this systemic and deep crisis, which deserves a strategic approach, policy decisions, single-mindedness, and learning.

Various studies indicate the following root causes: First, the government failed to strategically expand and diversify energy supply to support the economy's high growth and electricity accessibility in the post-apartheid period in the late 1990s. The *White Paper on the Republic of South Africa Energy Policy*, presented by the Department of Minerals and Energy in December 1998, unambiguously showed the changing external environment and the need for expanding and diversifying energy sources. It predicted that, with no timely investment, South Africa would soon have a deficit in electricity supply. No significant policy decisions or practical moves were taken, gradually leading to the first-ever blackout, or load shedding, in January 2008. The inability to transform the economy's overdependence on coal (over 90%), which account for 50% of Africa's greenhouse emissions, is a significant policy failure that contributed to the current crisis. Eskom's infrastructure has aged, with little maintenance, rehabilitation and investment in upholding its capacity.[30]

Second, Eskom faced a profound management and leadership crisis for over two decades, leaving it untransformed and unmodernised. Between 2007 and 2023, Eskom was under fifteen successive CEOs, showing the depth of the leadership crisis.[31] The board also suffered from a similar turnout, and Eskom had eight board chairs during the same period. The South African government's cabinet decides on Eskom's board appointment. The leadership

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[28] Presidency of the Republic of South Africa (2020).

[29] There is no accurate estimate of the economic damage. Some estimates show that the economy loses over R500 billion annually (over R1 billion daily) and over 2% of the economy.

[30] See Department of Minerals and Energy (1998); Lenoke (2017); Department of Public Enterprises (2019); Kessides (2020).

[31] The last CEO of Eskom, Andre de Ruyter, announced his resignation at the end of 2022 and left the institution in February 2023. Between 1985 and 2007, Eskom had only three CEOs and three board chairs.

instability created uncertainty, derailed strategic focus, and affected corporate governance and company performance. Significant reforms and turnaround in an organisation like Eskom would require continued, committed, and stable leadership for an extended period. The management and leadership crisis, which has persisted for an extended period, highlights the systemic problem in the selection and appointment of CEOs and board members, for which there is no substitute since it lies at the heart of corporate governance of any SOE. Political support for the executive leadership is essential during such crisis.

Moreover, alleged widespread corruption and maladministration became endemic.[32] The blurred lines of accountability and various government officials' interventions, further complicated the CEO's mandate. An essential responsibility of the government should be to create conditions that will allow stability and attract talented executives.

Third, as a giant and leading electricity utility provider in Africa, modernisation of the utility and business model management are critical. This would involve developing technological capability and reforming the business and management system.

An alternative business model of managing both public and private electricity utility has been the unbundling of the utility into electricity power generation, transmission and distribution, which does not necessitate privatisation. It allows the participation of diverse suppliers in power generation, while centralising transformation and distribution. There is also a need for research and development, as seen from lessons in China and Korea, which have SOEs and monopoly utility providers that are among the most sophisticated and highly efficient corporations.[33] The State Grid Corporation of China (CGCC) has 1.1 billion customers in the country. It generated an income of nearly US$400 billion in 2021, with 88% of total power consumption, supplemented by a few other utility distributors. In power generation, China deploys several SOEs linked to various energy sources.[34] Korean Electric Power Corporation, founded a century ago, has over 21 million customers, combines power generation, transmission and distribution, and operates internationally.

The Ministry of Finance announced debt relief for Eskom of R254 billion in 2022. The total debt of Eskom increased from R396 billion in December 2022 to R422 billion in mid-2023, indicating the company's worsening financial crisis and lack of creditworthiness.[35] The government has approved the unbundling of the power sector into three subsidiaries – power generation, transmission, and distribution, administered by three subsidiaries – in October

[32] See Swilling and Callaghan (2021) and the Zondo Commission Report (2022).
[33] The State Grid Corporation of China is investing in research on ultra-high voltage (UHV) transmission and smart grid technologies, and both have power wastage below 5%, which is considered highly efficient in the industry.
[34] China Huaneng Group, China Datang Corporation, China Huadian Corporation, and China Energy Investment Corporation are the largest power generators in China.
[35] See Presidency of the Republic of South Africa (2013, 2022, 2023); Sadiki (2015); Van der Merwe (2019); Swilling and Callaghan (2020); Trade and Industry Policy Strategies ([TIPS] 2022).

2023. However, this strategic decision is too late, and its execution will likely be complex. The answer to this entrenched catastrophe will neither be easy nor short-term.

The Eskom case is an archetypical case where crises become systemic and strategic, where too little and too late government decision could not reverse the collapse in performance threatening the legitimacy of the ruling party, leaving it with no clear pathway. Successful response and reversal would need unmatched political commitment to reform the sector and Eskom. This case shows that the root causes go beyond the state capture and standard corporate governance issues, and that privatisation is not necessarily a miracle medicine. The weaknesses in the country’s energy policy have contributed to the deep crisis in the sector, and Eskom has to grapple with the deepening crisis, such as the green energy transition or long-term investment in new energy sources. The debt burden of Eskom and the government’s grantees, while supportive of Eskom, brings forth huge liabilities and risks. In conclusion, the Eskom crisis does not have a quick fix and needs a strategic and longer-term approach.

## 3.2 The Case of the Ethiopian Electricity Power Corporation (EEPCO)

The Ethiopian Electricity Power Corporation (EEPCO) was established in 1955 during Imperial rule as the Ethiopian Electricity Power Authority (EELPA), with no separation of regulatory authority and utility provision. It was in 1997 that the organisation was restructured as a commercial entity, EEPCO, providing electricity utility and separated from the Ethiopian Electricity Agency, the regulatory agency. In 1991, the country’s power generation capacity was below 250 MW, with the distribution network limited to Addis Ababa and a few cities, and at 10% of universal access to electricity by 1999. The Ethiopian government pursued rural electrification and increased access to electricity, which grew from 10% to over 51% between 2000 and 2022, requiring enormous investment in power generation, transmission, and distribution infrastructure. The country’s rapid economic growth has called for a considerable increase in electricity, as shown in the annual demand growth of over 20% for over two decades.

Ethiopia relies on 100% renewable energy. The electricity sector and EEPCO enjoyed the government’s continued commitment under successive prime ministers. Power generation relied on hydropower, with limited diversification in other renewables after the 2010s. The price of electricity has always been subsidised, enabling access for both households and industries and one of the lowest tariffs worldwide, selling at about US 3 cents per KW hour until 2018, slowly increasing to US 4 cents in 2022. The government covered the resources for investment in new, large power plants and networks, given EEPCO’s inadequate revenue and profits. So the Ethiopian government used diverse sources of financing, mainly at concessional rates – making it the largest borrower of the Commercial Bank of Ethiopia (CBE) and external sources.[36] EEPCO leads the construction of Grand Ethiopia's Renaissance Dam (GERD), Africa's biggest dam generating 6 500 MW, entirely financed domestically.

The sector has a clear sector development policy, EEPCO's 25- to 30-year road map, and successive five-year development plans. Coordination issues are mainly resolved through constant and regular periodic reviews chaired by the Prime Minister, allowing timely decisions to be made and accountability. However, EEPCO's capability and executive performance have lagged behind the expansions and incurred delays and unmet demand.

In 2013, EEPCO was restructured into two companies: Ethiopian Electricity Power (EEP), which is responsible for power generation and transmission, and Ethiopian Electricity Utility (EEU), which is responsible for distribution. This strategic 'unbundling' policy was essential, but the implementation was complicated. The commercial and working relationship between EEP and EEU has been ineffective. An Indian company was hired for contract management of EEU to assist in reforming the distribution and retail services. Again, these reforms made limited progress.

The critical failures of these SOEs in the energy sector were: First, EEPCO could never catch up with the expansion of other infrastructure and industrial demands, often resulting in delays and additional costs in many projects, including the construction of industrial parks, railway networks, manufacturers and horticulture firms, thereby affecting exports. During the dry season, there were blackouts when the level of water in hydropower dams dropped. This weakness persisted for an extended period, highlighting the structural nature of the problem. Moreover, the corporation had to manage operations and services and the development of large-scale construction projects, putting it under enormous pressure. The internal organisation did not allow adequate focus on both priorities effectively. Operationally, the national grid was inefficient, with nearly 15% of national grid power wastage. In a nutshell, organisational and technological capability failed to catch up and did not receive adequate focus.

Second, corporate governance problems persisted, as the boundaries between the board of directors and the corporate CEO were blurred, leading to board approval of all procurement decisions and creating a conflict of interest in the board's supervisory obligations.[37] Although the tasks were challenging, the board had regular weekly meetings, which tied down the executive management time, indicating the erosion of trust in the CEO and the executive management team for ignoring the CEO's mandates. Third, the government's policy granted

[36] In 2014, EEPCO's domestics loans from CBE amounted to over Birr 110 billion, and over US$ 2.5 billion from foreign sources.

[37] The legal basis for all SOEs was laid by FDRE Public Enterprises Proclamation No. 25/1992 of the House of Peoples' Representatives in 1992, which had been well-functioning for the preceding 30 years (FDRE, 1992). The supervisory ministry appointed board members, the Prime Minister made the final decision, and the board included senior ministers.

the private sector's participation in power generation, while transmission and distribution remained under government monopoly with the aim to ensure electricity pricing and distribution serve the development goals. Nonetheless, EEPCO was never enthusiastic about private sector participation in power generation, and the government left the execution to EEPCO. The policy and regulatory framework for private sector involvement should have been completed before 2005, and is long overdue, showing the half-hearted execution of the policy.[38]

Fourth, a significant governance failure was on matters related to the contracting of Metals and Engineering Corporation (METEC), an SOE under the Ministry of Defence but restructured to serve industrial development established in 2010 under decree as an SOE). METEC's CEO sat on the board while it was a sub-contractor of EEP, leading to a conflict of interest and misguided decisions. In many procurement decisions, EEPCO was compelled to outsource projects to METEC despite fulfilling requirements in terms of cost and delivery. Fifth, issues of electricity pricing to households and industries were not based on a systematic analysis of how to manage the monopolistic position of EEPCO as a sole provider and put competitive pressure. There is limited evidence to show the long-term impact of the government's support in domestic and foreign financing and the effect of inflation and devaluation of ETB on loan servicing.

In conclusion, the case of Eskom and EEPCO illustrate how the government's policy decision could potentially impact—positively or negatively—the SOE's performance. It also shows that the energy sector is one of the most challenging sectors for most African governments, given the scale of required financial resources, the organisational and technological capability needed, the need for long-term strategies, and the transition to a carbon-neutral economy. Again, this case shows that the problem is not "ownership" but instead the pursuit of appropriate strategy and development of capabilities.

## 4. Aviation Industry and SOEs: A Showcase of International Competition

### 4.1 South African Airways and the Air Industry

This paper highlights that SOE performance has been mixed in different industries (such as finance, logistics, aviation, and telecommunications) and different national contexts, such as South Africa, a middle-income emerging economy, and a low-income developing country, Ethiopia. The drivers and causes of mixed performance vary across countries, industries and SOEs. The cases of South African Airways (SAA) and Ethiopian Airlines (EAL) are classic cases showing that corporate strategy, technological capability, and the industrial structure of the

[38] See Yalew (2022).

sector are essential drivers.[39] The paper illustrates that performance is not tightly tied to the ownership structure.

In the twentieth century, most airlines were SOEs, and all countries vigorously implemented protection of their flagship and managed it through bilateral air service agreements (BASA). However, a fundamental shift in the aviation and air industry – internationally and in Africa – that would shake the destiny of many airlines was under way in the 1990s. The air industry underwent significant liberalisation of the sky, deepening the intensity of international competition. With notable technological advances in commercial aircraft, the volume and scope of mobility of passengers and cargoes increased. As a result, many airlines were cutting their costs, improving efficiency, or expanding their destinations to stay competitive. Significant mergers and takeovers were happening across the globe.

Moreover, new entrants with a significant competitive advantage in scale and government support (such as Turkish Airlines, Emirates, Qatari Air and Etihad Airways) were entering the African market, particularly after 2000, and shaking up the African aviation industry. The air industry is capital intensive, and capacity utilisation and cost competitiveness are critical, requiring investment in airports and related infrastructure, and the building of organisational and technological capabilities is essential. Economies of scale, scope and diversification strategies are necessitated because of volatility and the seasonal nature of mobility. A key performance driver is the air industry's narrow latitude for poor performance due to intense competition, capital intensiveness, and implications for finance (where cash flow and creditworthiness are critical requirements).

To the surprise of South African policymakers and industry observers, SAA's financial crisis and operational difficulties in 2010 compelled the government to provide financial support. This downturn slowly led to it ceasing operations, with privatisation as a last resort. We observed dozens of large state-owned airlines, some considered national champions.[40] SAA was the most prominent African carrier until 2010, and was valued as a renowned brand and well-managed airline. However, SAA operated during the apartheid period to promote the economic and political interests of the apartheid regime and was protected from other carriers. Its mission was to support the government's 'self-reliance' motto under the international sanctions against the apartheid regime. With the end of apartheid in 1994, the ANC government had to take a strategic decision that redefined the purpose of SAA, and a strong government commitment to building it as a national champion would imply the fleet

[39] See Oqubay and Tesfachew (2019) on EAL's journey and technological capability. SAA and EAL were founded in 1934 and 1945, respectively. Also see Chilgenge (2016) and Nyatsumba (2021).

[40] For instance, among the high performers worldwide, Emirates, Qatari Airways, Turkish Airways and Singapore Airlines are state owned. Most of the European national carriers are partially state-owned. In contrast, any privately owned airlines have gone bankrupt or been taken over by other airlines. So, evidence suggest that the type of ownership is not a key determinant of the performance of firms in the aviation industry. Mentioning this point is relevant, because privatising SAA has dominated the coverage of South African media.

had to expand. This would require the strengthening of technological capability to successfully navigate increasingly intensifying international competition. The major carriers, such as Air Turkey, Qatar Airways and Emirates, had built significant scale and developed infrastructure. Evidence suggests that the South African government did not take a bold strategy on SAA, leading to subsequent incoherent policy responses.

In the 2010s, SAA faced major crises, leading it to bankruptcy. Under a new rescue plan, the government sold 51% of SAA's shares to Takatso Consortium in 2021, and it operated with nine commercial aircraft in 2023. SAA's subsidiaries, domestic operator Express and low-cost operator Mango, were in liquidation processes in 2023. The government was forced to provide significant subsidies to SAA in consecutive years.

The primary reasons that led to the downward spiral of SAA were: First, the weakness in government policy in putting SAA's role in South Africa's industrial policy and the lack of political will to build an internationally competitive airline that would play a significant role in South Africa's economic growth, including tourism, industrialisation, employment and service exports. As a result of this policy weakness and the lack of consideration of the changing landscape of the international and African aviation industry, resources and firms were not brought under a unified SOE to build the competitiveness of SAA. This policy gap did not lead to a proactive approach to making South Africa a primary tourism destination, building an aviation and logistics hub, and building industrial capacity in the aerospace and related sectors. The policy gap did not enable job creation (direct and indirect) or other spillover effects on the air industry.[41]

Second, SAA should have focused on building its technological and organisational capabilities and developing its competitive assets to ensure its high growth and international competitiveness in the face of the changing competitive structure of the aviation industry. Its capabilities comprise technological capability, organisational capability, fleet expansion, infrastructure development, and market development. The fleet expansion investment plan required a long-term perspective, extending over 10 to 15 years, sustained financial resources, and matching capabilities. SAA has yet to develop a new strategy to guide its long-term path.

Third, the management crisis at SAA was a primary cause of poor performance and contributed to a lack of strategic perspective. SAA faced a constant turnover of corporate and board leadership. Between 1998 and 2021, more than 12 CEOs and 12 board chairpersons were assigned, with an average tenure of less than two years. Corruption allegations have dominated the company in recent years, as underscored by the state capture report of South Africa.

[41] The direct jobs created by Ethiopian Airlines (EAL) reached 17 000, with 50 000 indirect jobs.

Moreover, unlike Eskom's operating environment, SAA's accountability to the Department of Public Enterprises as the supervisory agency and owner, and the sector's regulator, the Department of Transport, was not a binding constraint. Most SOEs in the aviation industry worldwide operate in a similar configuration involving government ministries representing the owner and the regulating body. However, a tourism development strategy, immigration policies and visa facilitation processes directly affect the passenger market, and weak coordination among the relevant stakeholders has affected SAA's performance and market negatively.

The crisis and bankruptcy of SAA were not because of government ownership. Few comparative cases are available in Africa's aviation industry. A significant weakness of African national carriers has been the inability to build adequate fleet size, technical and human capability, and the lack of a successful functioning strategy. Kenyan Airways could not boost its performance even after privatising its ownership to KLM Royal Dutch Airlines and hiring non-Kenyan CEOs. The political debate on Kenyan Airways continues without clarity on the root cause of its weak performance. RwandAir, the flagship carrier of Rwanda, was established in 2002 and commenced operation in 2003. It has made significant progress, thanks to the strong political commitment and consistent government policy on tourism and aviation, considering its role in a landlocked economy. It has invested in fleet expansion and human and technical capability, and has emulated Ethiopian Airlines in various aspects, including hiring the former CEO of EAL. Air Rwanda enjoys strong government support and has emerged as one of East Africa's best carriers, showing the importance of policy direction, the government's political commitment, and the need to develop the right strategy and investment in firm capability.

## 4.2 Ethiopian Airlines and the Aviation Industry

By 2023, Ethiopian Airlines (EAL) emerged as Africa's largest aviation group since 2014 and ranked among top 25 globally in 2022. It employed 17,000 employees and operated 150 commercial aircraft. EAL's revenue exceeded US$6 billion in 2022 and was Ethiopia's largest services export. It was vital for boosting the Ethiopian floriculture industry and the export sector. Multiple factors drove EAL's success as the most prominent African airline and an emerging high-growth company. First, founded in 1945, successive Ethiopian governments had unequivocally pursued a policy of positioning EAL as a national priority and at the heart of development strategy and, after 1991, it was given more strategic focus given Ethiopia's landlocked position and national security implications. It played a decisive role in developing Ethiopia's floriculture export sector and tourism sector. The government invested in airport infrastructure across the country, including 30 airports and terminals for tourism development that can also be used as air force bases. The airport and terminal investment was guided by a strategy to make Addis Ababa an aviation and logistics hub.

Second, from the early phase, the government pushed for Ethiopianisation (to replace expatriates in a protracted process), with the development of a highly skilled and professional workforce as its top priority. It established its aviation academy in 1956, which has grown to sophistication. EAL continuously invests in modernisation, organisational capability, and technical infrastructure. It also developed the largest logistics hub in Africa. In particular, after 2000 EAL developed Vision 2010 and Vision 2025, which enabled it to become Africa's largest airline in 2015. It expanded its fleet and long-range destinations and diversified into passenger and cargo fleets. It restructured itself as a holding company with seven diversified business units. It diversified into the hotel business, building a logistics company as a subsidiary through a joint venture with DHL Logistics. During the COVID crisis, when almost all airlines received government stimulus and bailout, EAL survived without any government subsidy (the government does not have the coffer to assist) and without any layoff of workers, proving its resilience and continued profitability. It adjusted its strategy to diversify its business model to focus on being a cargo freighter. EAL established its creditworthiness and never relied on the government treasury's guarantee. EAL's Vision 2035 aims to double the fleet and emerge among the top 15 airlines worldwide. It is the leading contributor of earnings from services export earnings.[42]

Third, EAL has enjoyed stability in its executive leadership by appointing a CEO and ensuring operational autonomy, enjoying direct access to the Prime Minister. The government has assigned an effective board functioning with independence and stability. Between 1990 and 2021, EAL had only four CEOs, all with aviation experience and promoted internally. It also had four board chairs, and the board's directors included two labour union representatives, along with independent members – mainly government officials with diverse professional backgrounds and retired aviation experts.[43] EAL has proactively engaged the various government agencies and the Ministry of Finance (representing the owner), the Ministry of Transport as a regulator, and the Ministry of Foreign Affairs as partners in working worldwide. The legal act for its establishment as an SOE has not been an obstacle to the smooth functioning of EAL for over 30 years.

However, the rise of EAL has always been dominated by tensions and conflict. In 2008, during the historic spike in oil prices, it had to join hands with the government and the horticulture producers/exporters association, to subsidise the floriculture sector a third each. EAL faced

[42] In 2019, before the COVID crisis, the services export earnings reached US$ 5 billion.

[43] The board adhered strictly to regular quarterly and annual performance reviews, and approved annual and five-year plans. It also undertakes a retreat for two to three days to review its strategic plan. Performance reviews and plans include a review of the global economy and aviation industry, and the industry's financial performance indicators are compared to three internationally top-ranked companies (such as Singapore Airlines, Lufthansa, Emirates, United). All procurement decisions are made by the CEO's teams, and the board's approval is required for the procurement of aircraft and its financing, a decision that is taken in the presence of a technical review committee, with representatives from the National Bank of Ethiopia and the Ministry of Finance assisting that macroeconomic risks are avoided.

the repatriation of its revenue from many African countries that faced a shortage of foreign currency. The relationship between the board and CEO always faced tensions, and the board was at times tempted to intervene in CEO mandates. In the mid-1990s, the board made blunders in efforts to restructure but lacked an understanding of the industry and assigned new members of the executives. This led to a crisis in EAL, and many technical and managerial executives left the airline. In the 1970s and 1980s, the government tried to intervene in industrial labour relations and advised the purchase of Antonov aircraft from the former USSR. This was rejected by the CEO, leading to a letter of resignation. It showed the government to reconsider its approach and avoid such measures. Successive CEOs have enjoyed direct access to the Prime Minister, which has enabled them to make timely decisions.

The above highlights that the government's political intervention is not necessarily evil, and that what matters is the purpose and nature of the intervention. It also shows how an airline can play a decisive role in a country's industrial policy, and that the public policy goal and commercial goals do not necessarily conflict. They potentially can contribute to the growth of the SOEs.

### 4.3 Summary

The story of SAA, EAL, and other African carriers highlights several insights into SOEs and development. First, the cases starkly show that ownership did not remotely matter for the performance of the SOEs. Second, the cases show that understanding the industry's trends, having a long-term direction, and developing a clear national strategy are essential for a thriving SOE sector. Third, capability development and technological learning are critical to boosting dynamic and competitive SOEs. As the aviation industry shows, an economy of scale and scope are essential in a globally competitive industry. Lastly, SOEs can play a prominent role in supporting development strategies in export industries.

## 5. Telecommunications, Banking, and Logistics Industries and SOEs

### 5.1 SOEs and Telecommunications SOEs

The telecommunication sector is critical in economic development and drives the digital economy. Technology has evolved rapidly and constantly, as typified by the expansion of mobile telecom systems, optic fibre networks, and the economic use of satellite networks. A critical challenge for SOEs is keeping pace and developing organisational capabilities with accelerated technological changes. The decreasing capital investment in emerging generations of telecommunication technologies (from 2G to 5G) in the last two decades enabled the private sector to take an active and leading role in this space. Foreign firms have expanded their operations in Africa and there are over fifty SOEs in the telecom sector, and most are profitable.

South Africa's Telkom was founded in 1991, with its roots in the Department of Posts and Telegraphs of 1910. In 2023, it had over 18 million subscribers. Telkom employed over 15 000 workers, generated revenue of ZAR 43 billion, and had over ZAR 61 billion in assets. Telkom operates in 38 African countries, highlighting its competitiveness and market expansion in an internationally competitive industry. The South African government allows multiple operators, and a transformed Telkom changed to have joint public-private ownership, in which the state retains 55%. Telkom dominates a significant market share in South Africa and has emerged as a valued brand. By doing this, the South African government has developed a competitive telecom industry. Here, the government's clarity on the policy of the telecommunication sector and its approach to the SOE have contributed to a successful outcome. The success of Telkom lies in the South African government's strategic decision to establish a telecom SOE, highlighting the role of government in building strategic industry at a crucial juncture. The government ensured that Telkom developed its capabilities, expanded its infrastructure, and maintained the industry's competitiveness. Given the rapidly changing technological innovations, and considering the private sector's role in the telecom industry, the government was convinced that it should mobilise additional resources by involving the private sector in joint ownership. Nonetheless, the government maintained a significant shareholding to influence strategic decisions. This proves the state's ability to build SOEs in a rapidly changing industry.

The Ethiopian government founded Ethio Telecom in 1894 as a government agency and it was a monopoly service provider until 2021. Its subscribers reached 70 million in 2023. The government adopted a policy that allowed Ethio Telecom to partner with foreign firms. Considering the country's vast land space and rural population, it was clear that private telecom operators were less likely to expand infrastructure to less profitable rural areas. After 2000, Ethio Telecom invested extensively in new national optic fibre and broadband infrastructure nationwide. This investment was covered through commercial and concessional loans, primarily secured with the government's guarantee. Ethio Telecom was not creditworthy enough to access external funding, putting a debt burden on the government in a highly profitable sector.[44]

Furthermore, unlike in the aviation sector, Ethio-Telecom was not adequately investing in its organisational capability and building its technological capacity. In 2010, Orange France was selected as a management contracting company of Ethio Telecom for two years. However, Ethio Telecom's strategy faltered in multiple ways. First, the management contract with the French telecom company to transform the organisation was only partially successful. A key

[44] Ethio Telecom employs 16 000 people and serves 56 million customers.

reason was a failure to assign competent professional corporate management that matched a technology company and dynamic industry. The board's complacency and weakness in focusing on organisational capability was the primary reason for not making a breakthrough. Second, another major failure was that Ethio Telecom never attempted to expand its regional and international operations, which would have put it under pressure to develop its competitiveness. Neither the government nor the corporation envisioned that it would become a regional player.

Consequently, Ethio Telecom's monopoly position was protected in the domestic market, and with no international operation, undermined its competitive position in a rapidly changing industry, and the quality and pricing of the service were severely rated. It lost a golden opportunity to emerge as a significant regional operator. The coverage by the internet and the depth of ICT in the country has been less impressive in contrast to many African peers such as Kenya. It was only after 2021 that the telecom sector was allowed multiple operators, hence losing an opportune moment. The government failed because it saw Ethio-Telecom as a 'cash cow' but did not focus on developing its technological and organisational capability and envisioning a competitive regional telecom company. From a 'cash cow' angle, the government could have generated similar revenues from licensing to multiple operators, or could have sealed a deal with a more prominent company through a joint venture. It never focused on building its technological capability and did not have an in-house R&D core. While state ownership was never the root cause, the primary failure was that the government allowed an incompetent telecom company to be protected. An opportunity for the telecom company to be a competitive regional player was missed.

### 5.2 Development Finance as Conduits of Developmentalism

Another critical industry in which SOEs play a prominent developmental role is banking, as evidenced by policy and development banks in Brazil (Bundes Bank), China (such as CDB and IDIC) and Singapore (DBS).[45] Several African countries have SOE banks – over fifty wholly or partially owned – mostly with modest performance and some playing critical developmental roles, such as the Development Bank of Mauritius. In addition, South Africa and Ethiopia have government-owned banks that have operated for almost a century. South Africa's Industrial Development Corporation (IDC) was founded in 1940 and is the leading development finance provider, supporting many industrial sectors. It has consistently shown robust performance, expanded its operation into other African countries, financed industrial projects, and views its mandate as lying within South African industrial policy. Under the Department of Trade and Industry, the IDC has focused on manufacturing, promoting job creation, supporting Black economic empowerment (BEE), and recently green energy – lending R16 billion in the past few years. Its lending to manufacturing was R8 billion in 2022. In 2023, the IDC's total assets

[45] CDB, the world's largest development bank, had total asset of 2.5 trillion dollars in 2023.

were R162 billion. The IDC approved nearly R20.7 billion and made a disbursement of R17.8 billion, lending a total of over R8 billion and approving about R21 billion.

The Development Bank of Southern Africa (DBSA), founded in 1983, primarily funds infrastructure development in SADC member countries and the Southern African region. It also finances local governments and municipalities. The South African Land and Agricultural Bank (or Land Bank) was founded in 1912 to support investment in agriculture. These banks have financed the priority sector, playing a developmental role. The three banks have acquired modest corporate governance levels and shown healthy financial performance (except the Land Bank's recent shaky position). These SOE banks could be significant sources of learning for other South African SOEs in different sectors, and other development banks in other African countries. However, these policy banks could benefit from learning from international benchmarks and world-class development banks like the Development Bank of Singapore, Brazil's Bundesbank, and China Development Bank, among others.

Ethiopia's two oldest banks, the Commercial Bank of Ethiopia (CBE) and the Development Bank of Ethiopia (DBE), were founded in 1942 and 1909, respectively. Both banks played the role of development banks, financing industrial and agriculture sectors despite the ambiguous name 'commercial' bank. The World Bank and IMF have pressured the Ethiopian government to break up CBE to end the dominance of state banks in the industry. CBE accounted for over 55% of assets, 70% of deposits, and 63% of total loans in the Ethiopian banking industry. While both are policy banks, CBE finances various sectors, including manufacturing, agriculture, public housing, real estate, and trading finance. It is also the largest financier of the state-owned electricity utility provider. CBE has also provided co-finance, with DBE, as a consortium in large-scale projects such as cement. Moreover, CBE played the leading role in boosting domestic savings by expanding its branches in the last 15 years, contributing to financing the GERD.

DBE, on the other hand, accounted for only 5% of the assets. The total assets of CBE and DBE were estimated to be approximately Birr 1.5 trillion.[46] DBE has been a minor player, but its lending was restricted to agriculture and manufacturing and its small asset base has been a major hindrance in its development financing; it has been less entrepreneurial and follows cumbersome bureaucratic procedures. DBE played a critical role in developing Ethiopia's export-oriented floriculture sector.

There is a complaint that the National Bank of Ethiopia micromanages and interferes unnecessarily. Despite the developmental policy roles, the backwardness of the banking industry limits its efficiency and performance. The decreasing exchange value of the Ethiopian Birr to foreign currency is a significant disincentive to investors and challenges many firms .

[46] CBE's total assets are over Birr 1.2 trillion (the equivalent of over US$ 28 billion), and DBE has approximately Birr 200 billion (over US$ 4 billion).

In summary, while the policy purpose has made an essential developmental contribution, the impact has been undermined by the banks' weak capitalisation and bureaucratic procedures and the unwarranted restrictions of the central bank, which aggravated the foreign exchange position. There is enormous space to modernise the SOE banks and play developmental roles, and the rationalisation of assets and focus are necessary. Making both banks provide loans to industries would require specialised knowledge about the sectors, as international experience shows, such as the Bundes Bank in Brazil or Netherlands's Rado Bank financing the horticulture sector.

## 5.3 Logistics Industry

In contrast, the SOEs in the logistics sector in Ethiopia and South Africa offer essential lessons for managing SOEs. With its origins dating back to 1860, Transnet was re-established as a leading logistics company comprising a merger of companies – port administration, railways, pipelines, and logistics services – offering a significant advantage in scale and scope. The merger was a strategic step in the right direction that could potentially lead Transnet to maximise its productivity and performance. It had assets worth over ZAR 355 billion and a revenue of ZAR 74 billion in 2018. It operates over 22 000 kilometres of rail infrastructure, manages the Cape Town, Durban and Port Elizabeth ports, and manages petroleum transport pipelines. It is one of the biggest employers, with 56 000 employees. Under Transnet's board, a new board was authorised to lead the Transnet Port Authority (TNPA), which has yet to be tested if it can boost performance. It owns 34 000 railway networks, eight commercial ports, and 3 800 km of petroleum pipelines.

Transnet has played an essential developmental role in boosting South Africa's domestic and international trade as Africa's largest economy. This favourable policy environment allows Transnet to provide a consolidated service. With many well-functioning ports, Transnet could emerge as one of the leading regional operators or even an international logistics player. However, Transnet's performance has deteriorated in recent years and it has become the prey of state capture and corruption, as reported by the Zondo Commission, and has carried a considerable debt burden. It has the opportunity to recover and transform itself, but requires the government's political ambition and commitment to build a competitive, world-class logistics operator, being the dominant player on the continent.

Ethiopian Shipping Lines (ESL) is the national shipping line and contributed to the economy until the 1990s. Still, its fleet did not expand with the size of the Ethiopian economy, and the company did not raise its scope of services. However, the corporation could not adequately support the government's export-led industrialisation strategy and did not rise as a competitive shipping line. Logistics costs and long delivery times were obstacles to the export and manufacturing sector, and the key logistics players (port, railway, shipping, transit) operated in a small and fragmented manner. A major obstacle was that the sector was closed to foreign and domestic private operators for an extended time, giving monopoly rights to

ESL and Ethiopian Maritime and Transit Services (EMTS). In the rapidly changing global logistics industry and the imperative that building an efficient supply chain and logistics is a driver of the export sector, allowing foreign logistics operators was an essential policy measure that was postponed for an extended period. A merger of SOEs in the logistics sector (namely Ethiopian Shipping Lines, Ethiopian Maritime and Transit Services, and Dry Port Enterprises) was effected in 2011, which was an essential but inadequate step. ESLC retained small shipping lines and made limited investment in its fleet and technological capabilities, which led to weak international competitiveness and limited contribution to the national economy, demanding urgent policy shift.

### 5.4 Summary

The three case studies provide a couple of insights. First, SOEs played an essential developmental role leading to the rise of the three industries discussed above, and the governments continue to play a dominant role despite changing environments. Second, the performance among the SOEs has been uneven, and variations remain an essential feature of firms' performance. Third, there is no evidence that ownership matters and that private ownership is superior to public ownership. Fourth, an economy of scale and international operations are essential drivers of building competitive SOEs, and government strategies on the specifics of each sector and the SOEs continue to be necessary.

# PART III: COMPARATIVE INSIGHTS, SYNTHESIS, AND REFORMING SOES

## 6. Comparative Insights and Synthesis of African SOEs

### 6.1 Developmental Mission and Productive Politics

This paper has explored the lessons from the continent by supporting multiple case studies drawn from several industries. First, the review shows that SOEs can play a strategic role in a country's development strategy and industrial policy. However, this demands building a thriving SOE sector and requires painstaking effort and a strategic approach. In South Africa and Ethiopia, many SOEs play such a role. In situations where this is not the case, such as the energy sector or Eskom, the price for failing to develop a productive and competitive firm is enormous. But there is no substitute, and 'privatisation' or 'independent power providers' is not an answer. Second, the paper shows that the governance of SOEs – both governing the SOE sector and corporate governance at the firm level – is critical. SOEs must respect legislation and practices; failing to improve governance can paralyse their performance. Third, effective SOEs surpass the government's political commitment and industrial policy. For firms to be competitive, significant investment should be made in organisational, operational, and technological capabilities, in line with industry trends.

Furthermore, through multiple cases, the paper shows that heterogeneity and diversity among SOEs are influenced significantly by issues related to the national context, sectoral features, the developmental and political nature of governments, and legacy issues. Mixed outcomes and unevenness are critical features of SOEs' performance. While many SOEs are in deep crisis, entailing formidable development challenges and political risks, there are also many SOEs that not only operate profitably, but also excel compared to private firms. The ownership structure is neither the primary nor the sole driver of performance, and a strategic direction should look beyond ownership or privatisation. However, heterogeneity and unevenness can be a source of learning – policy learning for government and technological learning for firms. Learning from international experiences and best practices is possible when it is purposeful and targeted.

What are the key lessons for national governments and SOEs, and complementary pathways to the future? This paper synthesises the key lessons from African SOEs, paths to the future, and lessons drawn from international experience. First, development experiences in Africa and worldwide show the importance of SOEs in advancing economic development and as a vital component of industrial policy. However, the practice shows that many SOEs continue with no policy rationale or purpose, some endured for historical reasons, and some because they were established without much thought. Nevertheless, it is also undoubtedly so that a poorly performing SOE sector will not contribute to the industrial policy goals and will be a waste of resources. Developing SOEs that are high-performing firms depends on the government's solid political commitment, willingness to pursue industrial policy and adherence to constant reform.

Second, in the governance of SOEs, the problem is not political interference *per se,* as often presented. As the owner of the public assets and leader of the developmental project, the state should provide direction and discipline for the SOEs, and ensure that public assets are used in conformance with the constitutional and legal requirements. The primary failure, as the South African and Ethiopian cases suggest, has been the inability to integrate with industrial policy perspectives and specify the developmental goals of each SOE. Even in cases where SOEs exist historically and are part of the legacy, a comprehensive study should be undertaken and associated policy decision made, as they need to be re-established with new purposes, merged with other SOEs or organisations, or have their ownership transferred. However, such a bold decision may have significant political implications, or may be unpopular in the public eye. Intentions are not enough, and the government should be disciplined in setting direction, enforcing policies, and delivering the best possible outcomes.

Third, the policy and commercial goals can complement each other, help virtuous growth and make a contribution. The key lesson is that without a *disciplined* developmental state, no SOE can emerge as a 'national champion' or 'national leader'. SOEs must receive 'intermediate assets', but the reciprocity principle should be strictly and consistently pursued to ensure that internationally competitive and productive SOEs are developed. This is possible, but is not a necessary outcome. As a policy direction, the government must focus on a few strategic SOEs that can play a catalytic role in the broader economy and set an example, rather than have a more significant number of SOEs that are not productive.

Finally, studies should be conducted regularly (every five years) to test whether the rationale and purpose of the SOEs require change. Many SOEs still need to meet this requirement, but have existed for a historical reason or as a pragmatic solution to fill gaps the private sector cannot deliver effectively. In this case, the government has to make a firm, well-thought-through decision, and such SOEs should be transferred into a transitional arrangement and restructuring of ownership. The rationale for this decision is not based on the fact that a private hand will improve performance. It is instead based on the fact that the state's resources and capacity are limited and have to be used for targeted purposes.

The government should enact a legislative framework that reflects the complexity of the SOE sector and international practices of administering and coordinating the SOE sector. Three crucial principle levers should be considered: ensuring developmental goals and public policies are achieved effectively, providing public assets and resources to generate maximum return and value, and benchmarking and implementing internationally applicable management systems and requirements. Maximising the achievement and delivery of this system is not a one-time task, but rather an ongoing process that involves learning and research.

## 6.2 Effective Governance Framework: An Essential Pathway

A productive SOE sector necessitates designing, implementing and continuously improving the governance system of SOEs, and this process has two dimensions – governing the SOE sector, which focuses on the bridge between government and the SOEs, and corporate governance within SOEs, which is essential for firms' high performance. In several African countries, governments apply different governance approaches, with limited effectiveness. Eskom is a notable example of how governance systems can further aggravate crises rather than help in a turnaround strategy, and then become fertile conditions for corruption. International experience in the governance of the SOE sector shows that many governments have moved from the decentralised governance of SOEs under various government ministries towards centralised management through specialised agencies. Decentralised governance lets various ministries administer SOEs following its sectoral nature. This was a dominant feature in many African countries until the 1990s. Ministries are compelled to combine regulatory and SOE responsibilities, which do not allow them to ensure that SOEs deliver on their policy missions and commercial goals. It also undermines the quality of regulating the sector.

### 6.2.1 Governance structure

A key priority relates to the type of coordination mechanism and structure used to monitor the SOEs. In several African countries, SOEs are administered mainly by multiple ministries, linked to some extent to past legacy. In this system, the SOE sector is fragmented under various government agencies, making it challenging to lead the SOE sector effectively. Practically, it is less productive than when SOEs are placed under the regulator ministry as a supervisory agency (the owner). There is an unavoidable conflict that cannot be resolved, and that damages both the commercial and operational performance of the SOE, and compromises regulatory mandates. Governments should be able to prevent this weakness.

A logical advance was to bring SOEs under a single government body, such as an agency or ministry (such as the Ministry of Public Enterprises in South Africa or the Ministry of Finance in Ethiopia). There are advantages and disadvantages regarding which supervisory body is effective, as this is also related to the prevailing power dynamics influenced by historical factors. Moreover, a hybrid system is followed by many African governments, making it challenging to manage SOEs by monitoring their performance and reforming the SOE sector in a coherent manner. Where this is not feasible, two or three coordinating agencies are mandated to administer SOEs (such as the Department of Public Enterprises, Department of Trade and Industry, and Ministry of Finance).[47]

In organising the centralised supervisory agency, two avenues are available: Establish independent holding companies (like TEMASEK in Singapore or SASAC in China) while giving the agency a high profile comparable to ministries (accountable to the President of Singapore or State Council in China) and empowering with sufficient power. A second option is to organise under the Ministry of Public Enterprises (as in South Africa and a few other countries) and make the minister a Council of Ministers or Cabinet member. This could burden the supervisory agency and encourage blurred responsibility, as the ministry has to make collective cabinet decisions and is susceptible to more frequent changes of appointees. The benefit of such a system is that the SOE sector is insulated from instability during cabinet restructuring after every national election. It also helps that the supervisory ministry is free from other political and government responsibilities (such as making cabinet decisions) and can focus on the professional management of the SOEs. In either case, the supervisory agency should have a highly sophisticated leadership understanding of the policy imperatives and corporate world, and a competent professional core to support the SOEs effectively. Which option could be most effective depends on the political structure and national experience.

[47] South African SOEs such as Eskom, Transnet and SAA are under the Department of Public Enterprises. The DBSA and Land Bank fall under the Department of Finance, while the IDS falls under the Department of Trade and Industry. See Matumba (2020), Kanyane & Samo (2021), Netswera, Fagbadebo & Dorasamy (2022), Parliament of Republic of South Africa (2005a, 2015a, 2015b)..

Lastly, maximum and continuous efforts should be put into identifying and improving the conflicts in the government's multiple roles as an owner (supervisory agency), regulator (competition law and sectoral regulation), and purchaser through public procurement methods. Nonetheless, this is an ongoing effort, and the conflict is not necessarily negative; what is critical is understanding the underlying causes (see Table 1).

**Table 1: Classification of SOEs based on characteristics**

| | |
|---|---|
| Development Finance (development and trade finance) | (a) This category includes policy banks such as development financing and trade financing (Exim banks). Development financing may specialise in industrial development, infrastructure development and agriculture, as in South Africa's IDS, DBSA, and Land Bank.<br>(b) It requires financial prudence, ensuring scale, portfolio balance, high ratings and sustainable financing.<br>(c) Requires an industrial policy targeting and selecting growth sectors, a specific bank policy for each industry, and involve targeted subsidy and performance requirements developed with the responsible government agencies.<br>(d) The involvement of the bank's representative in the management of firms may be relevant, depending on the specific industry and national context.<br>(e) Carbon neutrality and ensuring environmental and social safeguards have become essential.<br>(f) Close coordination with central banks, the Ministry of Finance, the focal policy and regulatory agencies, and placing development banks under a single government agency will help.<br>(g) Best examples that can be emulated include the Development Bank of Singapore (DBS), the Brazilian Development Bank (BNDES), and the China Development Bank (CDB). |
| Utilities, infrastructure, logistics | (a) Managing multiple stakeholders becomes critical, and interacting with dense provincial and local governments, individual customers – firms and households – becomes vital.<br>(b) Equity and inclusiveness become critical drivers in settling prices and ensuring minimum profitability and maximum cost recovery.<br>(c) Large workforce and decentralised service delivery.<br>(d) The need for extensive capital investment to expand infrastructure and upgrade and protect infrastructure.<br>(e) Ensuring environmental sustainability in infrastructure development and operation.<br>(f) Managing conflicts between commercial goals, policy goals and inclusiveness is a constant challenge. |
| Manufacturing and technology | (a) Economies of scale, scope, and international competitiveness are essential drivers.<br>(b) Productive and technological capability are of paramount importance.<br>(c) The increasing requirement to invest in innovation and research.<br>(d) Organisation along sectoral specialisation and diversification to related industries, and business partnership with international companies are critical.<br>(e) Industrial policy outcomes and long-term competitiveness override short-term profitability. |

### 6.2.2 Financial discipline

The review of African SOEs shows three aspects of inconsistent and harmful practices. First, many SOEs are under debt stress, and many SOEs have relied on the guarantee of the state (domestic and external loans) for an inadequate reason. In many cases, such decisions are made for political convenience and because of political pressure, often reinforcing the vicious cycle. Second, decisions related to the pricing and subsidy of services (particularly public utilities) are a significant fault line that is without policy direction considering all aspects. Subsidies are not isolated from costs to enable targeted support and measure performance. Increasing utility fees has political repercussions as it puts pressure on consumers, and consumers' voices also reinforce wastage and subsidise inefficiencies. The long-term macroeconomic impacts are not well considered. This critical policy area hampers the development of a highly productive SOE sector. The third aspect relates to the national government's obligation to ensure the inter-governmental relationship (such as between the electricity provider and rail transporter or between the electricity provider and municipalities – a typical example is the relationship between ESKOM and cities). The association must be based on a firm legal framework and conventionally acknowledged practices, rather than on short-term political convenience.

Ensuring that SOEs are structured under strategic business units or subsidiaries that operate on commercial terms and as profit centres promotes financial performance. A clear differentiation should be made in activities that require government subsidies, and the government must settle subsidies periodically to assist performance discipline. Maximising competitive pressure is essential, but the options are diverse and finding the optimum solution depends on multiple factors. Unbundling the electricity utility has been considered good practice, given the monopolistic nature of the utility. However, various ways of unbundling depend on numerous factors and the context of the country and sector.[48] These are issues that require a deeper understanding, research, piloting and phasing, and relating them to the national and sectoral context is essential for the best outcomes.

#### 6.2.3 Corporate governance within SOEs

In the African context, there is enormous scope for improving the corporate governance of SOEs, and the following recommendations are acknowledged to have an influence on improving governance and performance positively. The corporate governance within SOEs affects firm performance and ensures that the public asset generates wealth effectively and is utilised for the intended purposes. Effective corporate governance of SOEs has to underpin the national legislation, such as commercial or tax laws, to ensure the SOEs adhere to the existing rules and emerge as the best corporate citizens. Corporate governance should enable the improvement and maintenance of high performance, which is the ultimate purpose of corporate governance. There are various international lessons to improve corporate governance that can be a source of learning, such as the OECD's research, and publications

[48] The unbundling approaches of Ethiopia, China, Korea and South Africa all differ.

on SOEs.[49] The focus on *corporate governance* relates to the internal functioning of SOEs to ensure their mission is achieved, the expectations of key stakeholders are met, performance levels are improved, and a growth strategy is pursued. It is also to ensure that SOEs continuously upgrade their management systems and adhere to the principles of transparency (and disclosure of information) and accountability. Reviews of advances in corporate governance are a critical source of emulation and provide indicators, and specific international industrial practices play a crucial role in corporate governance. SOEs should be obliged to strictly follow the national laws and international standards applicable to business entities as the minimum requirement, and be encouraged to adopt international corporate governance practices constantly.

The first principle in corporate governance is ensuring strategic direction and respecting the principle of non-interference and operational autonomy, which, in reality, is a critical drawback and dilemma. However, this is the most common weakness in African SOEs and the following principles should be considered. First, the starting point is to ensure an accountable and competent board of directors. The board of directors is the supervisory body representing the owners. It appoints the firm's CEO and executive team and provides strategic leadership. The operational autonomy of the CEO is related to the type of board and membership, and a key obstacle in many African SOEs is the administrative intervention of the board or board chair, which undermines the CEO and the executive management.

Good corporate practices show that having a single level of board (rather than a board with two levels) is more effective in terms of accountability and maintenance performance, and the board should be appointed for a term reasonable enough to provide strategic leadership (Table 2). A five-year period is a realistic and better option than a shorter term of three years, and it should have the opportunity to extend it for a second term, which would enable continuity along with new members energising the board. An independent board chair, rather than the CEO serving as board chair, is a good practice that reduces conflicts of interest. Making the CEO a board member or non-member is widely practised in the corporate world. The board's composition must ensure that competent members are assigned, whether these be political appointees, business leaders, or specialists. The board's composition must be designed to understand the business environment, the specific industry, and the company's commercial and financial elements. The board of directors should have clear guidelines, and providing executive leadership training can strengthen the board's leadership. In many boards, a lack of stability and continuity is a significant obstacle. The root cause is often the flawed selection process and the absence of a well-planned succession scheme. The process to ensure that there is no conflict of interest is an essential principle in board composition and the board's decision-making. For instance, members should not be affiliated with

[49] The OECD has conducted research and issued publications on corporate governance, an essential source of lessons for African SOEs.

companies involved in business with the SOEs. This brings us to the role of the holding company or supervisory agency.[50]

**Table 2: Principles and practices considered good governance practices**

| | |
|---|---|
| State ownership | (a) Define the purpose, policy goals, prioritisation<br>(b) Ensuring the state is an 'informed and active owner'<br>(c) Ownership policy that specifies the rationale for state ownership, the government's role in the governance of SOEs, and the respective mandates of government bodies<br>(d) Ensuring operational autonomy and regular review of SOEs<br>(e) Oversight review by parliament sub-committees and cabinet |
| Board of directors and CEO | (a) Providing strategic direction on behalf of the owner with the necessary authority<br>(b) The board is independent, with separation of the Board Chair and CEO, and avoidance of conflicts of interest<br>(c) Worker representation on boards and members with diverse competencies<br>(d) The board should not interfere with the CEO's mandate<br>(e) Merit-based selection and appointment of CEO<br>(f) One-tier board system<br>(g) Internal auditor (under the executive management and board) and independent external auditor |
| Public policy and principles | (a) Subsidies related to policies should be financed by the state and made public<br>(b) Disclosure of SOE performance and assets<br>(c) Strict adherence to stakeholder value (shareholder, labour, creditors, community) rather than shareholder value<br>(d) No exemption from the application of government laws (such as tax or other standards) and access to financing |

Source: Own compilation.[51]

Secondly, the selection and appointment of the CEO and executive team are of strategic importance to the performance of the SOEs. The criteria for appointing the CEO should reflect the specific mission and role of the SOE, and the appointment should be based on the consideration of multiple candidates. The CEO should have full operational autonomy, and administrative interference by the board or chair must be prevented adequately and consistently. The board reviews the company's performance on a quarterly, bi-annual, or annual basis, and the board approves yearly plans and budgets. However, a smooth but functioning relationship depends upon various factors, and it is essential to create discussion forums allowing critical and constructive dialogue. A good practice to ensure autonomy and strategic leadership is to agree on a performance contract linked to performance-related incentives.

Third, another critical principle is maximising value to stakeholders rather than shareholder value. The various stakeholders, such as employees, creditors, shareholders, customers and

[50] See Department of Public Enterprises (2009, 2021); OECD and SOE Network for South Africa (2014); Presidency of the Republic of South Africa (2020). Ethiopia established a holding group, the Ethiopian Investment Group, to administer the large SOEs, but there is no conclusive evidence to show its impact on SOE performance (FDRE, 2022).

[51] See Asian Development Bank Institute (2017); OECD (2011, 2015a, 2015b, 2018, 2021); Wong (2018); International Finance Corporation ([IFC] 2019); Wezel and Carvalho (2022); Simone and Wang (n.d.); World Bank (2014, 2017, 2020, 2021).

suppliers, are essential to the long-term growth and performance of the firm. As a public organisation, the wider public and their representatives have a legitimate interest in seeing public assets used productively, and that the SOE is achieving its purpose. Hence, the SOEs should be stakeholders at the centre of their processes, involving consultations in their decisions and providing adequate information. An essential principle is maximising the level of transparency and ensuring accountability and, given the volatility of the global economy, ensuring that the firm manages risks. Good practices include ensuring that the external auditor is competent and has no conflict of interest. Firm performance must be made public regularly (annually), and constant communication must be maintained through adequate communication channels.

### 6.2.4 Firm capability, performance, and competitiveness

SOEs are commercial operators competing with other firms in their industry and in related sectors. Building highly productive and internationally competitive SOEs requires investing in strategies, operational and productive capability, technological capability, and organisational capability, and prioritising economies of scale and scope. Such a process demands constant learning, internalising new capabilities and competitive assets, and understanding the changing environment. First, as the cases show, African governments and SOEs do not focus adequately on building firm capability. SOEs are, first and foremost, firms that compete in the market – not just in domestic markets, but also in a constantly changing competitive landscape internationally. Even so, the firm-level capability determines its ultimate success and performance.

The number of globally competitive SOEs is limited in the African context, and the primary lessons should be that building vibrant and productive SOEs entails, first and foremost, developing the capabilities of firms, which will require a strategy for competitive assets specific to the sector and international in scope. The 'small is beautiful' view is unlikely to work in global markets, and rationalisation and mergers to operate at scale are essential. However, the issue is not about size *per se*, but rather the failure to focus on developing organisational and technological capability. Another puzzle for SOEs operating in 'natural monopoly' industries such as utilities is that competitive forces are insufficient to drive firm performance. However, various mechanisms are available to complement the competitive intensity, including a contrasting performance with the best performers in the industry globally, compelling the SOE to have an international operation to be used as a channel for international learning and performance comparison, and to form a strategic partnership with leading firms in the industry worldwide.

# 7. Reforming SOEs and Pathways to the Future

## 7.1 Strategic Approach to SOE Reform

In the 1980s and 1980s, the overriding agenda in many African countries was privatisation, with the false expectation that privatisation would perform a miracle on the ills of the SOE sector. However, evidence in Africa and elsewhere has shown that high performance is not tantamount to privatisation. In some contexts (such as South Africa), the conversation on SOEs has been dominated by 'state capture', which is crucial. Yet the performance of SOEs requires a strategic approach far beyond fighting systemic corruption and state capture to make them competitive and productive. Corporate governance issues were dominant in the 2010s (both in Africa and worldwide) as the economic contribution of SOEs increased in developing and emerging economies, and even in some OECD countries.

Furthermore, 'political interference' is raised as an obstacle to SOEs' performance. However, it is an illusion that SOEs can avoid political interference or political influence. Owners – shareholders, dominated mainly by family businesses – with a hands-on management style and intervention are a norm rather than an exception in private firms. A plausible notion is that the government has a 'constructive' political influence, yet there must be a condition that the SOE governance system does not tolerate administrative interference and corrupt practices. So, the issue is positive political impact rather than interference *per se*. The government, as owner, cannot be neutral to its stakes in its assets and SOEs.

Important lessons can be taken from countries that have engaged in developing productive SOEs. A classic example is Singapore's strategy that enabled it to build an effective governance system, productive SOE sectors aligned with the country's transformation agenda, and SOEs that excel in their industries. TEMASEK is the holding company, and it is accountable to Singapore's President to keep SOEs independent from the executive body's intervention and toe ensure accountability. Singapore Airlines, the Development Bank of Singapore and JTC Corporation are examples of SOEs that have become industry leaders and are competitive globally. The SOE reform in China has been at the heart of China's opening up and reform strategy, and yet it is a journey that has taken over four decades. While privatising the smaller SOEs and those not in 'strategic' sectors, China has single-mindedly focused on 100 national champions. Internationalisation of the SOE operation has been a critical strategy enabling economies of scale and diversification in related businesses. A long-term perspective directs the reform paths of Singapore and China, and reforms are part of the government's development strategy. Developing a competitive and vibrant SOE sector is a strategic mission requiring strong political commitment by the top leadership.

So, an essential takeaway is that the reform strategy must incorporate a transformative and developmental purpose, a robust governance system and exemplary corporate system, and sustained investment in firm capabilities. There is no shortcut to developing vibrant SOEs; it demands significant political commitment and policy clarity. Reforming SOEs is neither about privatisation, nor about a quick fix. It is not about zero political interference or interference limited to fighting corruption or cronyism. Reform is much more comprehensive and tied to a long-term strategic approach guided by national development goals. The situation of each SOE is relevant to designing appropriate strategies (see Table 3).

**Table 3: Approaches and strategies for performance improvement**

| Description | Focus |
|---|---|
| Firm capability and strategy | Firm capability<br>Firm strategy<br>Building industry-specific 'competitive assets' |
| Political and policy directions | National champions/global champions, a focus on building productive and technological capability<br>Redefining the rationale, purpose, roles and priority of SOEs<br>Responding to SOEs in crisis (high debt, financial crisis, mismanagement)<br>Rationalisation through mergers and restructuring, and transfer of non-strategic assets or SOEs through privatisation or to provincial and local government as a transition face<br>Strategic decision on the supervisory agency (the state as owner) through a holding company or single ministry |
| Manage conflict among competing goals | Financial goals (profitability, return on assets or economic value)<br>Operational goals<br>Public policy goals |
| Diagnostics of SOEs in crisis | Identifying and prioritising in terms of strategic importance, nature of the crisis, and urgency<br>Focus on addressing low-performing SOEs (but on the verge of crisis), strategies, and immediate actions to prevent situations<br>Turnaround strategies and policy reforms (how different between private and SOEs) |
| Furthering competitive and performance pressures | Which SOEs can leverage and benefit from listing IPOs (it may not be a solution)?<br>Reorientation towards the engagement of stakeholders as additional performance-enhancing pressure<br>Adopting performance review of international benchmarks |
| Pitfalls for disaster and performance collapse | (a) Approach to debt burden – both local banks and foreign loans under government guarantees, inter-governmental debts such as those owed to municipalities, inter-SOE credits<br>(b) Interference in procurement by the government, including preferential policies that are not transparent or harm the tendering SOEs (such as decisions on contracting to non-performing SOEs)<br>(c) The loose approach to establishing new SOEs<br>(d) Decisions that relate to managing subsidy and pricing |

## 7.2 SOEs as a National Transformation Project

In many African countries, despite the diversity of contexts, governments have a compelling rationale to prioritise energy, development finance or policy banks, and the development of industrial infrastructure (parks), given the role they can play in industrialisation, green transformation, building productive capability, and economic transformation.[52] It could be

[52] See Oqubay (2015); Cramer et al. (2020).

necessary to prioritise and manage ailing SOEs and to apply a turnaround strategy. However, the responses may need to be revised or preferred for various reasons. The depth of the problem necessitates critical government policy measures, such as issues related to debt stress or energy policies beyond the SOE mandate. Given the nature of the emergency and the responsible government, bodies have to make timely decisions in a coordinated manner. On debt issues, the Ministry of Finance, the Ministry of Public Enterprises and central banks may need to coordinate their decisions and implementation. In some sectors, the supervisory and regulatory ministries need to work together. In aviation, a coordinated effort between transport and tourism ministries and immigration agencies will be necessary.

Building vibrant SOEs should aim for additional measures. First, SOEs play a significant role in advancing the government's transformation agenda. They have to pursue their mandated developmental purposes and are expected to deliver the policy goals, operate as competitive commercial organisations, and adapt to external and industry trends. A good example is climate change and environmental sustainability, and firms must pursue green growth and contribute to a carbon-neutral economy. This pushes the SOEs to contribute to green transition and excel in their industry, building new competitive advantages in an ever-changing landscape. Second, a critical policy direction could be that SOEs must develop an in-house research and development capability to boost their technological and innovation capability, play a crucial role in the national innovation system and invest in their innovation capability. The reform strategy is expected to address the SOEs' existing challenges and strategic plans. Third, classifying the SOEs into three critical types from the perspective of their purpose, and prioritising from the deepness of the crisis is crucial. Which SOEs are to be developed as national champions? Which ones play a transitory role (five to 10 years), and which may not be essential in the long term? Which ones should be relinquished through various mechanisms, including ownership restructuring?

Lastly, diversity and heterogeneity are the key features of African SOEs driven by their national context, sectoral structure and circumstance, firm history, level of economic development and options available. This has implications for the reform agenda, implying that a differentiated direction is essential, and a 'one-size-fits-all' prescriptive approach is unlikely to succeed. The mixed outcomes and unevenness could also be used to drive performance, and as a source of learning. Systematic research on SOEs and the use of technical advisory councils could assist the reform agenda if the mandates are clearly defined.

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## Appendix 1: Lessons from EAL's corporate governance and firm capability

| Description | Focus and priority |
|---|---|
| Corporate strategy | Vision 2010: It achieved US$1 billion in revenue.<br>Vision 2025: It became Africa's largest carrier by 2015 and significantly expanded and diversified into diverse business models.<br>Vision 2035: Emerge as the world class airline, doubling its current fleet from 150 to 300.<br>Capability development is the key strategy: human capital, technological capability, fleet modernisation, and infrastructure (cargo terminal, passenger terminals, etc.).<br>Lesson: SOEs must have ambitions for long-term growth strategy and invest in firm capability. |
| Scale | The fleet size of both passenger and cargo fleet expanded.<br>EAL has one of the most extensive domestic, African, and global destinations, giving it advantages in scale.<br>A merger of Ethiopian Airport Enterprise and the transfer of 30 airports and related infrastructure under EAL. |
| Corporate governance – finance | Strict discipline of finance, a requirement to access international capital markets.<br>Cashflow and liquidity comprise a crucial financial strategy.<br>Creditworthy: Nearly 50% of the investment in its fleet and infrastructure is financed from the capital market without government guarantee.<br>All subsidiaries are organised as strategic business units and profit centres. |
| Corporate governance – plan | Annual goals and performance indicators are set and reviewed regularly.<br>Performance-based incentives and bonuses are used. |
| Corporate board | The board of directors reviews corporate performance quarterly, semi-annually and annually.<br>Strategic plan review conducted every one to two years.<br>Interference in executive matters is discouraged.<br>No government ministries are permitted to intervene in its corporate matters (except the supervisory ministry).<br>The board approves the procurement of aircraft. |
| Corporate governance – CEO | The CEO has direct access to the Prime Minister.<br>Discussion with the board is thorough and the CEO constantly updates the board.<br>Labour union is represented via two board members. |
| Coping with Covid-19 | It reviewed and adapted its strategy to the new environment, delaying growth investment programmes.<br>EAL remained profitable during COVID-19 and did not request government rescue.<br>It diverted its business to cargo when passenger transport froze. Nearly 30 passenger aircraft were converted to cargo, boosting cargo productivity.<br>Diversification to new businesses (such as investment in hotels) was pursued.<br>No employees were laid off, and no salary and benefits were cut. Employees doubled their commitment to support the survival of EAL. |
| Capability | EAL constantly invested in its aviation academy from the 1960s.<br>The aviation academy is world-class and one of the most prominent worldwide – training pilots, technicians, cabin crew, and corporate officers.<br>The academy has been upgraded into an aviation university. It generates revenue from external services.<br>Over US$ 100 million investment was made in a school for cabin crew. |

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