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### The Changing Role of Government: The Reform of Public Services in Developing Countries

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## CHAPTER 6: WORKING WITH PRIVATE PARTNERS

**Batley, R and Larbi, G., 'Working with Private Partners', in *The Changing Role of Government: The reform of public services in developing countries, 2004*, Palgrave Macmillan (reproduced with permission of Palgrave Macmillan).**

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### The case for privatizing management

The previous two chapters described reforms *within* public management. In some respects these have 'imported' market approaches and values into the public sector. In this chapter we examine the experience of 'exporting' functions to the private sector, and the impact this has on the functioning of public administration. Whether through the import of practices or the export of functions, these can be seen as different ways of addressing the principal-agent problem of public administration. That there is such a problem will be accepted for the purposes of this chapter, although it can well be counter-argued that this critique of public administration is less a description of reality and more a mobilizing device to generate impetus for reform (Salamon 2002, Joshi and Moore 2002).

Lane (2000) represents the principal-agent problem and alternative routes to its reform on two dimensions as in Table 6.1. In the classical form of public administration, politicians are at the hub of two relationships. First, they receive the demands of citizens (their electorate) and, second, they fund bureaucracies through taxation to supply the response. Principal-agent problems arise in both relationships: citizens have weak control over politicians, and politicians have weak control over lengthy bureaucratic hierarchies. The public bureau (the supposed 'agent') may exercise power over the public and the politicians whom it should serve, based on its compulsory funding (taxation), its monopoly status, and the long-term contractual security of permanent employment. By contrast, it is argued that a firm is truly an agent because, in a competitive market, it is governed by shareholders' search for profit and by consumers' choice and willingness to pay.

Some of the management reforms described in Chapter 4 and 5 involved a shift from type I to type II in Table 6.1. In those cases, the public service remains the direct provider, paid for out of taxation, but, in the shift to type II, managers are made accountable for their performance within shorter-term contractual agreements instead of having long-term employment contracts within the public service.

The approaches described in this chapter add the second dimension of reform identified by Lane. They seek to change also the tax-versus-charges axis, towards types III and IV. They put the provider onto a more wholly marketized

footing, with short-term contracts *and* payment for services rendered. However, this may stop short of full privatization: government may retain ownership of assets, the service may be charged to clients or government may itself finance private providers out of taxation. The important point is that accountability of providers to government or to citizens is made more direct; the World Bank (2004) describes this as strengthening shorter routes of accountability.

**Table 6.1: From bureaucratic administration to charging, short-term contracts and the market**

<b>Contracting on the demand side</b>		<b>Contracting on the supply side</b>	
		<b>Long term</b>	<b>Short term</b>
	<b>Taxes</b>	I Bureau	II Internal markets, agencies
	<b>Charges</b>	III Concessions, vouchers	IV Firm

Source: Based on Lane (2000, p. 193)

The cases of private participation referred to in this and the following chapters range from the complete privatization of the ownership of assets, through the contracting or licensing by government of private operators, to the private financing of public services by investors. The term 'private participation' is used because in almost all cases there is a mixture of public and private roles. Usually, the private partner assumes the function of directly providing or producing the service while government keeps overall indirect responsibility for ensuring that the service is delivered adequately. Indirect roles include tasks such as analyzing policy options, setting standards and monitoring their enforcement, raising and allocating finance, managing budgets, contracting, regulating and creating incentives for private producers (see Chapter 1). Under these forms of provision, government retains responsibility for the protection of the public interest while service managers are freed from the constraints of public administration and exposed to the competitive pressures of the market.

The goal orientation of public leaders, in principle, is to the satisfaction of the 'public interest', that is to the wider social interest rather than to private ends. Interpretations of what is in the public interest arise from a complex amalgam of institutionalized practices and political competing demands. Public management therefore involves a balancing of multiple objectives, including changing (and perhaps conflicting) policy goals, efficiency and equity in delivery, due process and legality in procedures of operation. Procedures are supposed to be open, transparent and subject to scrutiny. They have therefore to be based on institutionalized rules that govern ways of operating both internally in the management of staff and other agencies, and externally in relation to the public. Public organizations are also rule-based in relation to each other; they are supposed to coordinate under the authority of government, respecting each other's spheres of responsibility (Lane 2000 Chapter 7, Du Gay 2000).

While these features of public administration are necessary to the core policy-making functions of government, they are widely thought not to be appropriate to the management of service delivery. They give no encouragement to operational flexibility, few or no incentives for the achievement of results and efficient use of resources, and rarely any clear basis of accountability for performance. They are also held to divert resources towards people with influence and away from the poor (Devarajan and Reinikka 2002, World Bank 1997 and 2004). One response has been to clarify the roles of public service managers by giving them more defined responsibilities, within semi-autonomous units but still within the public sector. Such reforms were analyzed in the previous chapters.

Marketizing the delivery of public services is seen by its advocates as further freeing managers from the encumbrance of public service conditions (World Bank 1997, p.87). Within the framework of commercial contracts, goals and objectives can be specified, and managers freed to act flexibly and entrepreneurially to achieve given ends, focusing on the satisfaction of consumers rather than obedience to rules of procedure. Principal-agent relations are clarified through more direct and specific contractual relations between government (as principal) and independent operators (as agents).

This does not remove the case for public administration but shifts it back from service delivery to the management of other deliverers: the public interest, policy objectives, transparency and coordination are now to be achieved by contract, monitoring and regulation.

"After a decade where there has been a focus on ways of reducing the role of government in the economy, there is now recognition that a smaller role for government in the direct provision of services may mean a bigger role for government in policy development, co-ordination and regulation." (Bennett and Mills 1998).

Ideally, public-private relationships combine the virtues of both public administration and of private management. But, this can only be true if the public and private partners have the capacity to perform their new roles. The danger is that the efficiency gains from contracting the private or voluntary sectors may be outweighed by the additional transaction costs of doing business between multiple actors. Setting policy frameworks, coordinating, contracting and monitoring come at a price. If the price is higher than the gain, then there is a better case for the full integration of the service within either the public or private sectors.

This and the following chapters examine how far such models of public service reform are being applied in developing countries, whether their application differs between sectors, what roles are implied for government, and how far they are constrained by the capacity of governments and their private partners.

## **Organizational arrangements for service provision**

Privatization in the sense of complete divestiture has applied mainly not to public services but to the 'productive' and competitive activities that were previously organized as state-owned enterprises. State ownership of commerce, industry, agricultural production and marketing was common but has been internationally largely undone, often under pressure of structural adjustment (see Chapter 3). However, even in these productive sectors, the dismantling of state ownership has often been accompanied by the emergence of new roles for the state in advising, promoting, enabling or regulating the non-government sector. The grounds for government's continued involvement is that there is a residual public interest whether in developing market providers or in restraining the impact of the market. Some examples will be examined in Chapter 8.

From the beginning of the 1990s, a further wave of reform began to affect developing countries - for the transfer of the delivery of social and infrastructural services to the private and community or NGO sectors (Odle 1993, Adam et al 1993, Cook and Kirkpatrick 1995, Batley 1996). The first candidates included services such as street cleaning, waste collection, road maintenance, parks, hospital cleaning, catering, security guards, and public utilities such as water and power supply, airports and ports. Later candidates for liberalizing reform were the social services, particularly health and education. These were often difficult cases to undertake since they frequently confronted political and ideological objections as well as being technically difficult to put out to contract or to regulate. They often affected basic human needs or strategic national resources, involved large groups of public sector workers, were key spheres of political influence, and were undoubted areas of 'market failure' that required some level of state intervention (see Chapter 1, Box 1.1).

Apart from a few countries such as the UK and Chile, the complete privatization of social and infrastructural services is rare. Much more common is some sort of contractual relationship where government retains ownership and control, while the private or NGO sectors take on operational roles subject to public control. Under these arrangements, private firms or NGOs are invited to tender for a contract or licence let by a government organization. The contract or licence may be small-scale and short-term for a specific activity financed by government, or large-scale and long-term where the contractor finances and manages an entire government function (such as the delivery of water supplies).

Recognition that there is not a straight and simple choice between public and private provision opens up the possibility of combining the two sectors in various organizational arrangements. These can be seen as alternative ways of allocating the risks and responsibilities of ownership, financing, operation and maintenance between government and private or community operators (World Bank 1994 and 1997, Savas 1987 and 2000).

Table 6.2 shows how ownership and the financing and operating functions may be split between public and private or non-governmental sectors, and gives examples drawn from the research<sup>1</sup>. The cells in light gray indicate the functions performed by the public sector; the more heavily shaded cells identify those functions where there are shared public and private responsibilities; and the white cells those where the private sector, NGOs or users take on roles. Under different organizational arrangements for service delivery, government and the private sector<sup>2</sup> retain different degrees of responsibility for the ownership of assets, for financing investment and operations and for managing operations.

The main possible organizational arrangements for service delivery are described more fully in Box 6.1. On a scale of declining government control, they range from the pure public management of services, through various levels of contracting of functions to the private sector, through the licensing and regulation of private activity, to informal arrangements of joint venture and collaboration. With regard to the state's role across this range of possible arrangements, there are four main ways in which it may be involved:

1. The state directly *provides* services, owning, operating and financing operations without private involvement
2. The state *purchases* the services of contractors
3. The state *licenses and regulates* private, NGO or community providers
4. The state *collaborates* with private, NGO or community providers through formal or informal joint arrangements.

This and the next two chapters are concerned primarily with 2 and 3, where government seeks to exercise its responsibility indirectly but retaining authority. This chapter sets out the case for the alternative arrangements, considering how the nature of services and the capacity of actors may influence choice between them. The following two chapters look at the experience of contracting and regulating non-government service providers in the four research sectors.

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<sup>1</sup> See Batley 1996, Nickson and Franceys 2003, Plummer 2002, World Bank 1994 and 1997 for fuller explanation.

<sup>2</sup> 'Private sector' is here taken to include NGO and user or community provision.

### **Box 6.1 Public-private organizational arrangements**

#### ***Pure public service delivery***

- Government owns, finances and directly delivers services. Particular one-off works or supplies may be purchased from contractors.

#### ***Public ownership and finance with limited private operation***

- Government retains ownership of and responsibility for service provision but finances private providers to give particular support services through management or service contracts.

#### ***Public ownership, some private finance and private operation***

Under these arrangements, government passes responsibility to the private sector for the production and delivery of the service and has ultimate ownership of the assets, with the following differences

- Lease: the contractor finances the operation of the service from revenue, whilst government covers investment costs
- Concession: the contractor finances the operation of the service and investment costs from revenue
- Build-operate-transfer: the contractor finances the operation of the service and investment costs from revenue, and retains ownership until the end of the contract.

#### ***Private ownership, financing and operation under government regulation or support***

- Provision and financing of a monopoly service by private owner/operators under licence, with regulation by government,
- Competition between government-licensed private producers or deliverers of the service,
- Government financial support of private consumption and provision, through, for example, subsidies, vouchers or loans.

#### ***Co-production***

- Joint venture: Formal partnership between independent public and private providers through joint ownership, joint ventures and investment,
- Informal understanding between organized groups of citizens/clients and state agencies to make resource contributions to the joint production of a service.

**Table 6.2 Distribution of Functions in Different Organizational Arrangements**

<b>Contract type (typical duration)</b>	<b>Asset ownership</b>	<b>Capital financing (investment)</b>	<b>Current financing (operations)</b>	<b>Tariff collection</b>	<b>System operation</b>	<b>Types of activity</b>	<b>Example from case studies</b>
Works/supplies contract (one-off)	Public	Public	Public	Public	Public with private inputs	One-off -e.g. building or supplies	Drug supply
Service contract (< 3 years)	Public	Public	Public	Public	Private for specific services	Specific technical task	Hospital cleaning, water billing
Management contract (3-5 years)	Public	Public	Public	Public or private	Private	Management tasks over a short period	Water company management
Lease contract (affermage) (10-12 years)	Public	Public	Private from revenue	Private	Private	Extended operation and maintenance contract	Water supply
Build-operate-transfer (BOT) (20-30 years)	Private to public	Private debt repaid by revenue	Private from revenue	Private	Private	Major investment projects	Grain mill
Concession (20-30 years)	Public	Private debt repaid by revenue	Private from revenue	Private	Private	As lease, with responsibility for investment	Water supply, Food storage
Joint venture (indefinite)	Public and private	Public and/or private	Public and/or private	Public and/or private	Public and/or private	Infrastructure and development	Business and agricultural services
Co-production	Public and users	Public and/or users	Public and/or users	Public and/or users	Public and/or users	Local infrastructure and development	
Licensed NGO or charity	NGO/charity	NGO/charity, maybe with public subsidy	NGO/charity, maybe with public subsidy	NGO/charity	NGO/charity	Under contract or licence, especially in social service	Mission hospitals
Licensed private firm	Private	Private	Private, maybe with public subsidy	Private	Private	Private operation of services, under licence	Medical practitioners





## **The application of public-private arrangements for service delivery**

Before looking at real cases of contracting in the next chapter, this section indicates how and why, in principle, alternative organizational arrangements may be appropriate to different public services. It adopts an essentially technical approach, suggesting a correspondence between the characteristics of services and how they might be organized. It focuses on four broad categories of organizational arrangement - contracting out, lease and concession, licence, and joint venture or partnership.

### ***Contracting out***

Within the framework of public ownership, there is the contracting of services paid for by the public sector. This may be through one-off contracts, or fixed period service or management contracts. Being relatively short-term and specific, they safeguard the interest of the public authority, which retains its control over the delivery of the service. These arrangements are therefore likely to be appropriate where there is a strong public interest and government does not wish to cede its responsibility because it has little confidence in its ability to handle long-term contracts. This may apply, for example, in situations of monopoly, or where there are strong equity considerations, or where there are important effects not only on direct consumers but also on wider society (see Box 1, Chapter 1). On the other hand, piecemeal contracts may have the disadvantage of creating problems of fragmentation and difficulties of coordination. These arrangements are therefore most easily manageable where tasks are naturally divisible and discrete: for example, construction and maintenance works, neighbourhood services, refuse collection, ancillary services in the health sector, and aspects of internal administration such as billing, salary payments and vehicle maintenance.

### ***Lease and concession of monopolies***

Lease and concession contracts are longer-term arrangements that allocate managerial and financial responsibility to the private sector. In leases, the contractor covers running costs from revenue; in concessions, it must also finance investment in fixed plant. They are ways of managing natural monopolies whilst avoiding the concentration of power in either the public or private sectors. They achieve this end by separating the direct and indirect aspects of provision, subjecting the private producer to public contractual control. They are most clearly applicable to non-public goods with a monopoly tendency and where there is sufficient public interest (on grounds of welfare or external effects) to justify continued public ownership. Examples are the public utilities (water, electricity, gas) and collective services such as refuse incineration, bus terminals and municipal market management.

Build-operate-transfer schemes can be seen as a variation of lease and concession contracts, where the primary purpose is to achieve the construction of a

particular capital investment project, rather than to manage the system. The investor designs, finances and builds an asset - for example, a highway or a water production and transmission system. The investor then operates the asset for typically 25-30 years, in return for payments made by government, or sometimes by the users; after that period the asset is transferred to the government body.

### ***Licensed competition between producers***

Licensed or regulated competition between producers is technically appropriate to 'private goods', that is those which it is possible to charge for and which individuals compete to consume. The argument for public intervention is not so strong as to demand direct public sector entry into the production or delivery of the service. In the absence of monopoly, the case for government intervention might rest either on the need to promote equitable access or to mitigate the effects of unrestrained competition on society at large. An example of the first sort would be the management of bus transport to ensure that an entire city is covered at similar tariffs; of the second that market stall-holders fulfil basic health requirements or that builders comply with building regulations.

There are many cases where government licenses private providers but also keeps a stake as a direct provider itself. This applies particularly in the case of 'merit goods', where there is a policy commitment to equitable access and government seeks to guarantee this by itself offering the service. Basic education and health are common cases of this sort. In other services, raising less profound equity issues, governments sometimes use licensing as a step towards reducing their direct role in service delivery.

### ***Joint venture or partnership***

Several sorts of joint arrangement can be identified where state agencies and private bodies act in a mutual endeavour, with or without joint ownership. Public-private partnership in joint ownership or investment schemes is most likely to occur where there is a strong possibility that opportunities for private investors will be generated by government involvement. The public sector's contribution might be either to undertake necessary investments which private firms are unable to perform (due to their large scale, high risk, or difficulty of charging to consumers) or to facilitate private action (by covering risk or using the coercive powers of the state). Typical circumstances would be the acquisition of land and the installation of infrastructure for social housing and commercial development.

Joint venture companies are at the formal end of the spectrum. Government enters into contractual relationships with the private sector both in setting up the company and in awarding the joint company the contract to undertake the work. Unlike pure contracting out or concession arrangements, there is the complication that government participates on both sides of the contract, leading to possible conflicts of interest: government is there to ensure the public interest but also has an interest in the contracting companies' gains.

Apart from the collaboration of public and private sector investors, another possibility is that the beneficiaries of public services may participate in their production and delivery. Again the possibilities of user participation range from the more formal and contractual to the more informal and casual. Cooperatives formalize the ownership by the beneficiaries of the organization that supplies the service, as in the case of the water systems in Santa Cruz, Bolivia (Nickson and Vargas 2002). More common are looser arrangements where users collectively contribute to the management of a service in some form of institutionalized agreement that is not legally binding or formalized. The term 'co-production' has been coined to define these looser arrangements where the lines between state agencies and non-state actors are blurred (Ostrom 1997, Joshi and Moore 2003).

### **Matching organizational arrangements to capacity**

There are risks and costs to be set against the possible advantages of public-private partnerships. Successful contracting depends upon there being genuine competition between competent firms, social control to guard against nepotism, and governmental capacity to specify and enforce contracts. Where the conditions exist, contractual arrangements may make for efficiency; but the conditions are exacting. Weak public administrations may lack the capacity to undertake the new (indirect) roles which follow from contractual arrangements: setting broad frameworks of policy, managing contracts, regulating providers, financing and supporting providers and consumers. If they fail to do so, particularly in the case of monopoly services, the situation may be worse than under direct public provision. The transaction costs of making and monitoring contracts may not be justified by the possible efficiency gains in service provision.

Factors to consider in assessing governmental capacity to manage contractual relations with private partners can be summarized as

- The characteristics of the service
- The complexity of alternative contractual relationships
- The capacity of government and the contractors to manage the relationship
- The institutional environment.

These factors inter-relate as Chapter 7 will show. Different types of service are more or less suited to alternative contractual arrangements that require different degrees of capacity on the part of government and contractors. Moreover,

capacities have to be deployed within an institutional environment that may either support or limit the conditions for effective public-private working. Institutional factors include the stability of the economy and the political system, the functioning of the judicial and financial systems, and the relationships between government and the business sector. As the World Bank (1994 and 1997) implicitly suggests, there is an uncomfortable conundrum: precisely in those countries where the public provision of services has failed, the conditions for effective private participation are likely also to be absent. The Bank's answer is to select for private involvement first those services that present least problem for contracting whilst also building government's capacity to manage more complex cases (World Bank 1997, p.97).

### ***The effect of service characteristics on the ease of contracting***

Chapter 3 described some of the characteristics of service sectors and how these may affect the balance of power between principals and agents, or, in this case, governments and contractors. Among these, Williamson (1987) has described three factors that determine the ease of contracting:

- The degree to which the service can be specified in advance: Is it possible to adequately specify the requirements to which the contractor is subject? This is more difficult in the case of services where the objectives are multiple, long-term, non-measurable or qualitative - for example social or health services.
- The degree of asset specificity: Are the assets (equipment, knowledge) required by the contractor so specific to the contract that choice is limited and the winning contractor can hold government to ransom? Large scale infrastructure investments (for example in the water sector) or highly professional or technological services in the health sector present this sort of problem.
- The practicality of gathering and measuring information about performance: Is the contractor's performance measurable? Does government have the capacity to gather the information that it needs in order to monitor contract compliance? Information asymmetry in favour of the private provider may lead to 'regulatory capture', where the provider effectively controls the public regulator. Information gathering and assessment may be a general problem for a weakly organized government but is particularly likely to arise in the case of social (including health) and professional advisory services where goals are difficult to quantify and measure.

The greater the difficulty of specifying and measuring performance, the more the principal will have difficulty in controlling the agent according to simple contractual rules. The argument then grows for a relationship between principal and agent that is more based on understanding than on specified contractual commitments. On the other hand, if the contract becomes too loose, it will reduce the pressures on the contracting agent to act efficiently.

### ***The effect of contract types***

Different types of contract present different sorts of cost or capacity constraint. In principle, the risks to the contracting body and the contractor rise with the growing duration and complexity of contracts (Williamson 1975). Short-term, simple contracts where the object of exchange is discrete, present relatively low risk to the principal (the contracting agency) and to the agent (the contractor) who can more easily agree about the terms and outputs they expect, without concern that conditions and requirements may change over time. Short-term, service or management contracts for specific inputs are more likely to be specifiable and measurable. On the other hand, they present an opposite problem: a total service would have to be composed of many sub-contracts to specialist companies. This presents problems of high transaction costs in designing contracts, and coordinating and monitoring contractors.

Longer term and more complex arrangements, such as concessions, have the advantage of wrapping all aspects of the service into one contract over a long period, potentially cutting transaction costs. On the other hand, the design of such contracts requires a great deal of information and experience to anticipate the relationships between all the elements of the service and to try to anticipate all the possible risks and uncertainties that may occur during the term of the contract. Since no written agreement can foresee everything that may happen over a 20-30 year period, long-term contracts are likely to be 'relational' - based on sufficient mutual trust and understanding to allow for adjustment to circumstances (Walsh 1995, p.136). Sako (1992) describes these as 'obligational contractual relationships' by comparison with the 'adversarial contractual relationships' that try to specify all possible eventualities in legal terms on the assumption that the partners seek to outwit each other (Flynn 1997). Trust may be injected into a contractual relationship by resorting to a third party, an independent regulator, in whom the partners both have confidence. In such a mediated relationship, the regulator should fairly recognize both the goals of the contracting body and the requirements of the contractor to remain viable.

Particularly in the context of developing countries, all these issues are in question: the existence of trust between partners, the ability to handle complex contract design and management, and the conditions for disinterested regulation.

### ***The capacity of partners***

Apart from the characteristics of the service and the complexity of different contract types, there is also the capacity of the partners to manage contractual relationships between public and private partners. On the side of the private contractors the following questions arise:

- Are there alternative possible providers with adequate capacity to undertake service provision? Are there enough possible contractors to provoke competition? Can contracts be specified (broken down) in such a way as to maximize opportunities for small and large contractors to compete?

On the side of government:

- Does it have the skills and organization to make and monitor contracts?
- Are the necessary instruments for contract enforcement available, for example by legal compliance or by the threat of affecting contractors' reputation by divulging information on their performance? Can government exercise them?

Where contracting is undertaken in the absence of the necessary conditions, the danger and likelihood is the emergence of inefficient and even corrupt relationships. Two studies of contracting out in Kumasi and Accra in Ghana illustrate the problem, in what might be thought to be the simplest of services - public toilet management. Even in these very small-value contracts and even where the conditions exist for competition, political practices have encouraged a lack of transparency in contract allocation and refusal by contractors to pay revenues to the municipality (King, Inkoom and Abrampah 2000, Crook 2002). Chapter 7 will explore this question further.

### ***Experience of private sector involvement in the case countries***

So far, this chapter has assumed a rational planning model in which decisions about alternative organizational arrangements are made on the basis of service characteristics and the capacities of governments and contractors. This was a way of describing the alternatives and of identifying the factors that allow them to function. However, as Chapter 3 showed, history, institutions and vested interests are more important than rational planning in explaining reforms, particularly in the conditions of developing countries. As a prelude to the following chapters, which look at specific experiences of contracting and regulating, this section outlines the broad patterns of liberalizing reform and private sector involvement that have taken place in the research countries. The countries include Ghana, Zimbabwe, India, Sri Lanka and several 'reference countries' in Africa, Asia and Latin America, and the focus is the four service sectors that were studied.

#### ***Business support***

The fullest government withdrawal from direct provision is in the industrial sector, achieved through a combination of divestiture, privatization and closure of unprofitable state enterprises. The textiles and garments industries were selected for study because, in most countries, they were among the first to develop under state protection and the first to be 'de-statized'. Governments have now almost wholly shifted from the role of direct production of yarns, fabrics and garments

and very largely also from regulatory and licensing roles. From state production and control of the private sector, governments have shifted towards attempting to deliver support services to the private sector - engendering a favourable policy framework, market analysis and promotion.

Having dismantled its own import licensing function, the Ghanaian Ministry of Industry and Commerce has tried to adjust to giving technical advice to firms it had previously regulated. In Zimbabwe, the Ministry of Finance together with donors opted to create a semi-autonomous Zimbabwe Investment Centre out of parts of ministries. Completely autonomous support organizations (for export promotion and information support) were set up with their own or donor funding in Ghana and Zimbabwe. In India, among a vast number of trade-related and semi-autonomous industrial research and training institutions, some gained a new lease of life as the government released its controlling grip. From the end of the 1970s, Sri Lanka created a series of agencies to promote inward investment, developing a significant and internationally linked textile sector almost from nothing. The research examined the operation of these agencies intended to promote and facilitate private firms in the four countries - these are described in Chapter 8.

#### *Agricultural marketing*

The policy goal in most countries is to liberalize agricultural trade and promote a market economy. Progress has been relatively fast in *external* trade under pressure of international competition - for example, in meat and cotton marketing in Zimbabwe and cocoa purchase and export in Ghana. However, *domestic* trade in staple grains has often remained protected and controlled by governments, particularly in India and Sri Lanka. The growth of private trading and private services to farmers has often occurred, not as a result of policy, but as the private sector fills gaps left by the failure of government schemes. Government bodies have tended to cede ground to the private sector through their decline rather than by the planned restructuring of public intervention.

Apart from the unplanned growth of private services, two types of relationship with the private sector were found. First, particularly in the export trade, governments have sought to strengthen their support roles to traders and farmers, for example by regulating the quality of cocoa exports in Ghana. Second, they have contracted the private sector to provide specific inputs to government-managed services, for example grain storage in Sri Lanka and India, maize exporting and transportation in Kenya. Government bodies have frequently tried to hold on to their support roles in agricultural marketing, contracting inputs from the private sector, rather than putting entire services out to the market.

#### *Urban water supply*

Internationally, urban drinking water is a case of radical reform. Private firms are increasingly being brought into the financing, construction and operation of water systems through short and long-term contracts. However, reform in the four core



countries was more limited, with the partial exception of Ghana where there were proposals for establishing lease arrangements for urban water supply. In India, Sri Lanka and Zimbabwe, reform mainly involved the changes *within* the public sector that were examined in Chapters 4 and 5: increasing the autonomy of state agencies, decentralizing water supply to local government, strengthening management, operating on a commercial basis and establishing new approaches to regulation. The pressure on state-owned utilities to operate more efficiently had led some to contract out specific functions to the private sector - for example, meter-reading, billing and managing pumping stations.

The water sector offers a range of types of contract - service and management contracts, lease, concession, and build-operate-transfer - that will be analysed in Chapter 7. But, the research had to go beyond the four core countries to examine the more radical cases of privatized management, in Argentina, Chile, Malaysia, the Philippines, South Africa, Trinidad and Tobago. The major research question is whether such reforms can operate in poorer countries.

### *Health care*

The broad structure of curative health services as between the public and private sectors remains largely unchanged by reform in the four core countries. The private sector is dominant in primary and informal care and is, at best, weakly regulated, while the public sector is dominant in hospital and formal provision. The main reforms again largely focus on re-structuring within the public sector - decentralization from and reorganization of ministries of health - rather than in changing its role. With regard to private providers, policy statements declare the intention to improve regulatory frameworks, to support private sector development and to contract out services but are weakly implemented in most cases.

On paper, there has been more radical reform in the African than in the Asian cases with proposals for the contracting out of support and clinical services. Subsidies to non-profit (church) hospitals were also common in Africa. However, in practice, the Asian countries, including Thailand, presented more examples of successful contracting out. These appeared to be less rooted in (donor-led) ideology and more in pragmatic decisions than in the African countries. Contracting is much more often of support services than of the clinical aspects of health as Chapter 7 will show.

## **Conclusion**

Public administered services face two principal-agent problems: citizens have weak control over policy-makers, and policy-makers have weak control over lengthy bureaucratic hierarchies. Theory suggests that introducing the private sector into the delivery of public services can help to overcome these problems. This may be by full privatization, or government may retain ownership of assets, and itself contract and finance private providers out of taxation. By putting the

provider (the agent) onto a marketized footing, under contract and with payment for services rendered, the citizen and policy-maker (the principals) are given more control over the performance of agents. Within the framework of a contract, goals and objectives can be specified, and managers are freed to act flexibly and entrepreneurially to achieve given ends.

Full privatization, in the sense of complete divestiture, has applied mainly in the productive sectors - industry, agriculture and commerce. The complete privatization of social and infrastructural services is rare. Much more common is some sort of contractual relationship where government retains ownership and control, while private firms or non-governmental organizations deliver all or part of the service. Under different contractual arrangements, government and the private sector retain different degrees of responsibility for the ownership of assets, for financing investment and operations and for managing operations.

There are technical grounds why different arrangements may be suitable to the provision of different services:- contracting out where tasks are naturally divisible and discrete; lease and concession where services have a monopolistic tendency; licensing where government needs to promote equitable access or to mitigate the effects of unrestrained competition; and joint ventures where there are complementary interests between the public and private sectors.

However, the judgement about whether and how to contract depends also on the capacity of government and private partners to handle alternative contractual relationships. Services where it is difficult to specify the desired outputs (for example, because they are qualitative) and to gather information to measure their effects are intrinsically the more difficult to contract. Short-term contracts may be easier to agree and to monitor and less risky than long-term concessions but, on the other hand, they may impose higher management costs on government. Governments may or may not have the skills and organizational capacity to design and implement contracts, and the private sector to compete for them. The capacity of the partners will in its turn be influenced by the context in which they operate - for example, the degree of political and economic stability and respect for the rule of law.

The real decisions of government to engage in one or the other form of partnership with private firms depend on the history and institutions of particular countries and of particular service sectors within countries. This chapter has described the broad pattern of liberalization in the research countries. The industrial sector and external agricultural trade are generally the most fully liberalized, while formal urban water supply and health care remain more resistant to change. However, in all cases there is a tendency to move towards a stronger involvement of private service providers. Chapter 7 goes on to examine the experience of contracting out services to the private sector, while Chapter 8 examines how governments regulate and enable private providers.