EFFICIENCY-BASED RESTRUCTURING APPROACH OF ROMANIAN ECONOMY

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Abstract

Large-scale corporate restructuring made necessary by a financial crisis is one of the most daunting challenges faced by economic policymakers. The financial crisis at the end of 2008 has brought back , in the Romanian economy too, the problem of the negative economic growth, of the massive interenterprise arrears and the huge losses of the business operators (this time,privately owned) as well as the need for restructuring not only of the residual state portfolio or government entities, but also for the private sector through the means of market economy.

A comprehensive strategy and methodology for restructuring, encompassing both the corporate and financial sectors, is put in place once the economic crisis in Romania is judged to be systemic in scope. The extent of the restructuring, the required resources and timing became the critical issues. These issues are and were compounded by contention for scarce resources, lack of legal framework, lack of expertise within the Romanian enterprises and inefficiencies resulting from the activity being carried out across the economy by various entities. The actions that will be taken have to be justified on a cost - benefit basis and measured to ensure that the desired results are achieved within a certain timeframe setting-up the concept of "Efficiency-Based Restructuring". This concept was tested and proved to be competitive, during the large scale restructuring process of the mid nineties in Romania.

Keywords: restructuring, liquidation, corporate governance, privatization, economic crisis
JEL classification: D21, D24, G28, G32, L33, O16.

1. INTRODUCTION

Corporate restructuring on a large scale is usually made necessary by a systemic financial crisis – defined as a severe disruption of financial markets that, by impairing their ability to function, has large and adverse effects on the economy. The intertwining of the corporate and financial sectors that defines a systemic crisis requires that the restructuring address both sectors together.

The last decade of the past century was dominated by paradigmatic controversy on the sequences of restructuring and privatization processes. The economy was registering suboptimal economic performances characterized by severe declines in the GDP; huge losses of the state-owned companies, and huge interenterprise arrears that accounted for over 35% of Romania's GDP.

The solutions that I designed, implemented, coordinated, managed and measured in my capacity of macro decision-maker of the time (starting with 1993) focused on a "top-down" model of restructuring, which precedes the privatization process and were institutionalized and included in common governmental and international financial institutions programs (such as IMF, IBRD, and EBRD, etc).

The results of the implementation of Restructuring Programmes between 1993-1998 might be short-listed in the following actions:

- The shutting down of producion capacities in value of 600 milion dollars;
- The sales of assets of approximately 50 milions $;
- Staff reduction of approximately 35.000 people

Additional measures:

- Funds worth 170 million $ from SOF for modernization and technology upgrading;
- Bank credits worth 300 million $;
- State budget allocation worth 75 million $ from the financial recovery fund destined both to energy and gas payments and to severance payments totaling 6 salaries to the staff downsized

For these measures as well as for those addressd to conciliation, the estimated economic effects will be materialized in:

- Cost reductions (400 million $);
- Cash-in improvements (600 million $);

Synthetically, the results of the conciliation process of the commercial companies that signed the conciliation agreements are as follows:

- Of the total debts of 1 blllion $ 71% were reconciliated
- Of the total conciliated debts of 710 million $, 71.8% represent reschedueld debts to the suppliers, banks and the state budget. 0.5% represent the reduced payment of the debts to the suppliers, banks and the state buget and 27.7% represent cancellation of penalties granted by the suppliers, banks and the state budget

As a result of the „ shock policies" from that time, the state budget had been cleaned of a series of hidden or quasi-fiscal elements such as credits aimeied for the agricultural sector, indirect subsidies for the heavy industry obtained from the foreign exchange restrictions, and subsidies for consumers through regulated prices for energy and agricultural sectors. As a consequence, the increasing trend of public deficits from 1993-1996 had been stopped.

From 1999 until 2009,the topics of arrears and losses of the state companies have disappeared from the current economic disscussion and were substituted by the ones referring to the accelerated process of privatization.

The launch of the financial crisis at the end of 2008 has brought back , through different alarm levels registered, the problem of the negative economic growth, of the massive interenterprise arrears and the huge losses of the business operators (this time,privately owned) as well as the need for restructuring not only of the residual state portfolio or government entities, but also for the private sector through the means of market economy.

Successful government-led corporate restructuring policies usually follow a sequence. First, the government should formulate macroeconomic and legal policies that lay the foundation for successful restructuring. After that, financial restructuring must start to establish the proper incentives for banks to take a role in restructuring and get credit flowing again. Only then can corporate restructuring begin in earnest with the separating out of the viable from nonviable corporations – restructuring the former and liquidating the latter. The main government-led corporate restructuring tools are:

- mediation
- incentive schemes
- bank recapitalization
- asset management companies
- the appointment of directors to lead the restructuring

After achieving its goals, the government must cut back its intervention in support of restructuring.

2. EFFICIENCY-BASED RESTRUCTURING

Successful restructuring is not possible without a strong foundation established by government action across the spectrum of economic policies.

- First, overall economic stability must be entrenched to provide the confidence needed for debt restructuring. Stable prices, interest rates, and exchange rates are needed for debtors, creditors, and potential investors to have enough certainty to do business.
- The scale and nature of corporate distress must be quickly assessed by the authorities, banks, and advisers to determine if the problems are systemic and thus whether the government should take a leading role. The assessment of corporate distress can be based on quick calculations of the debt servicing capacity of the aggregate corporate sector, the demand for bank credit, increases in nonperforming loans, and bankruptcies.
- A comprehensive strategy for restructuring, encompassing both the corporate and financial sectors, should be drawn up as soon as possible once the crisis is judged to be systemic in scope. The involvement of all interested parties in the formulation of the strategy enhances its credibility, as does transparent presentation of its objectives, tasks, and methods of implementation. Sweden, during its banking crisis of the early 1990s, and Korea, in 1997 – 1998, benefited from the early formulation of comprehensive restructuring strategies.
- A supportive legal, regulatory, and accounting environment is necessary for successful corporate restructuring. Important legal aspects of restructuring include foreclosure standards, foreign investment rules, and merger and acquisition policies. Regulations governing debt-equity conversions and asset sales often need to be changed to make possible novel and complex restructuring transactions.
- Corporate governance must be brought up to international standards to provide incentives for viable firms to restructure their balance sheets and maximize their value. Improved governance is needed not only to push managers to restructure the existing debt stock, but also to operate profitably and improve future profit flows. Often liberalization of foreign investment can promote good governance through the importing of international best practices.
- Closing nonviable corporations will incur social costs that may require offsetting government actions to help the poor and to maintain political support for restructuring. Hungary and Poland took measures to reduce income disparities in the mid-1990s, which reflected more than just corporate restructuring, albeit with mixed success. In East Asia, rudimentary social safety nets at the time of the 1997 Asian financial crisis were expanded to offset the impact of the crises on the poor through income transfers,

unemployment-limiting measures, and measures to maintain access by the poor to social services. Social measures should be formulated with the cooperation of corporations and unions.

In the case of Romanian enterprises it is well understood that there is a need for restructuring in state-owned companies due to the losses registered, level of technology, cost of working capital, energy costs, etc.Not only this, but in latest agreement signed with IMF, he so-called “precautionary-agreement”, in order to have access to the promised 3,4 bil.Euro,the matrix of conditionalities provide précised targets for restructuring or liquidation.

The extent of the restructuring, the required resources and timing become the critical issues. Feasibility studies and debates over "Pre-Privatization" restructuring vs. "Post--Privatization" restructuring should be shelved and applying the "80 / 20 Rule" becomes necessary. Simplistically, this means that if you can quickly implement a subset of actions that have the potential to achieve a large part of your overall objectives, you should incrementally proceed and worry about the residual as you go forward.

This is the essence of "Efficiency-Based Restructuring” which we proposed as a methodology and generic theme to be applied to this activity by all involved – either in managing the process or implementing the needed changes.

Efficiency-Based Restructuring requires that any actions are justified on a cost / benefit basis and measured to ensure that the desired results are achieved within a certain timeframe.

The first task of financial restructuring is to separate out the viable from the nonviable financial institutions to the extent possible. To do this work, financing and technical assistance from international financial institutions can be helpful.

Corporate restructuring can begin only when is distinguishing viable from nonviable corporations. Nonviable corporations are those whose liquidation value is greater than their value as a going concern, taking into account potential restructuring costs, the "equilibrium" exchange rate, and interest rates. The closure of nonviable firms ensures that they do not absorb credit or worsen bank losses. However, the identification of nonviable corporations is complicated by the poor overall performance of the corporate sector during and just after the crisis. Viable and nonviable firms can be identified using profit simulations and balance sheet projections, as well as best judgment.

Liquidating nonviable corporations during a systemic crisis usually requires the standard court-based bankruptcy procedures.

The government must also decide on disposal of the assets of liquidated corporations. Delays in asset disposal tie up economic resources, slow economic recovery, and impede corporate restructuring.

The balance sheets of viable corporations must be restructured. Restructuring will involve private domestic and foreign creditors, newly state-owned creditors, and asset management corporations, as well as stakeholders such as unions and governments. Usually, balance sheet restructuring takes place through the reduction of debt or through the conversion of debt into equity.

Financial incentives through a preset government-financed scheme can help if corporate distress is systemic, market or regulatory failures inhibit restructuring, and the government has adequate fiscal resources at hand. These schemes usually involve insurance or subsidy incentives made available to creditors and debtors on a voluntary basis.

The need for the government to first expand and then shrink its role helps explain the long time needed to complete restructuring. The new restructuring institutions are subject to economic and political constraints that force the government to weigh difficult tradeoffs, especially between restructuring's short-term costs (unemployment, dramatic falls in asset prices, learning curve of new corporate managers, for example) and long-term benefits (improved resource allocation, and safer balance sheets).

The time needed to complete restructuring can be shortened if the strategy is properly designed. As noted earlier, early and transparent formulation of an overall strategy can build public support, counter the resistance of vested interest groups, and improve policy effectiveness. Rapid establishment of a supporting legal environment is essential. A clear statement of the restructuring goals makes it plain later on when the government should pare back its role and shut down restructuring institutions. Sunset provisions for government restructuring institutions can help limit their life-spans.

3. RESTRUCTURING – ACHIEVING COMMERCIAL VIABILITY THROUGH MANAGED CHANCE

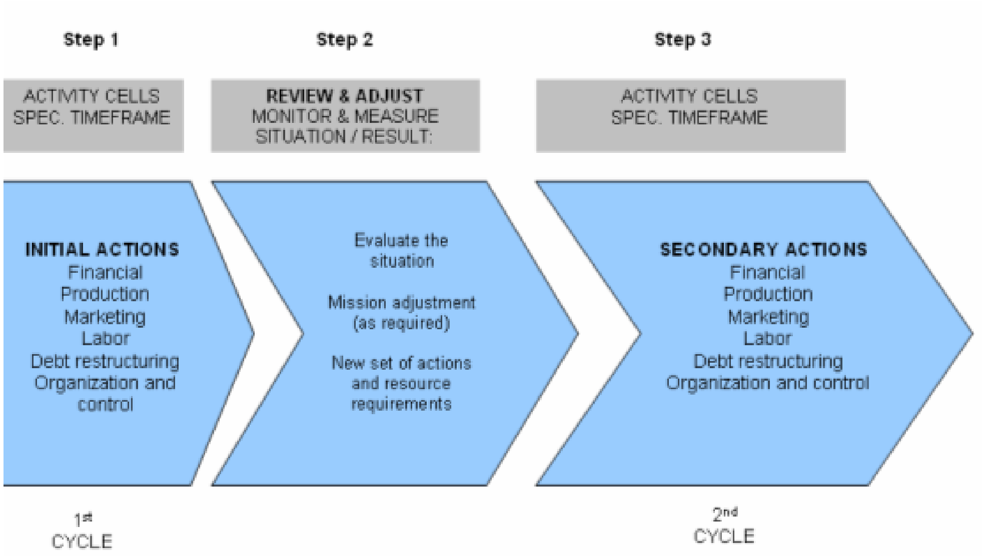

Figure no. 1 Short-term action plan (STAP's) cycles: Incremental implementation of comprehensive restructuring programs

Definition: Restructuring a commercial activity implies change – change in the way a company creates value and delivers that value in the form of goods or services to a marketplace.

The determination of the degree and focus of any such changes, as well as the implementation of the actions necessary to create change, is difficult and carries certain risks. Therefore, restructuring is a serious undertaking and must be managed accordingly.

It requires, up front, a commitment to the activity on the part of the enterprise management and any stakeholders.

As evidence of this commitment, all enterprise management, regardless of the financial condition of their company, should have in place an on-going program to systematically review, from a "zero base", the values generated by each activity in their company. This generally is done, at a minimum, each year during the budgeting and business plan process. It should be recognized that this is difficult in companies such as SOE's without cost accounting systems and profit center definition.

However, unpredictable changes in an economy in general and the respective competitive market of an enterprise in particular, will require this assessment to be carried out more frequently.

This periodic evaluation of business activities will nearly always demonstrate the need for some adjustment in the way business is conducted – both in terms of internal operations and the manner in which the company interfaces with the market.

This process of "mid-course assessment and adjustments", as management navigates down a critical path defined in a business plan, will translate over time into a restructured business.

The success of a business is fundamentally measured in how well management carries out this process – and indeed, the long term commercial viability of an enterprise is dependent on the ability of management to implement the changes needed to optimize its strengths and minimizes its weaknesses.

This makes it necessary for the manager to have:

a) a well-defined program of actions to be implemented along
b) a critical path
c) short term and long term priorities identified.

Additionally, in overseeing the process of change, implicit in any restructuring program, a manager can benefit from another simple rule: "SITUATION – MISSION – - ACTION" – i.e.:

(1) periodically reviewing a business situation,
(2) adjusting the business activity to a realistic set of objectives and
(3) implementing an appropriate set of actions.

Iterations of this basic rule of management are simply periodic reviews of the business situation that has developed as a result of the short-term actions that have been implemented.

If the situation has improved or deteriorated, the objectives should be either maintained or realistically adjusted and an appropriate set of next steps would be implemented.

By repeating this process, a manager can control the restructuring process and reduce the risks associated with change of operations.

4. ENTERPISE LEVEL RESTRUCTURING

Restructuring previous State Owned Enterprises (SOE's) is very different from restructuring a fully "commercialized' company.

Management of previous SOE's are generally production-oriented professionals accustomed to having their mission defined by a centralized authority that was also responsible for providing resources.

Management's mission in an SOE was largely to control the process of delivery per specifications defined from outside the enterprise.

Restructuring at the enterprise level requires management to implement difficult and sensitive actions, to make strategic choices and to incrementally assess progress.

For the management of a previous SOE, this would not be a familiar process and is further complicated by the lack of expertise and over-hanging government policies. Therefore, it is essential that the enterprise manager implements what is achievable without outside intervention and quickly build momentum on cost control and improving liquidity pending the change in policy and / or the acquisition of outside resources.

The identification of what is achievable and then taking charge of a plan of action is fundamental to the concept of "Efficiency-Based Restructuring".

It must begin with an understanding of some of the immediate short term actions that should be undertaken as well as what strategic changes are necessary over the long-term to re-tool corporate culture, management infrastructure and other important elements of the business.

As examples of immediate and long-term changes, the following outline is useful in organizing and mobilizing the restructuring of a commercial activity.

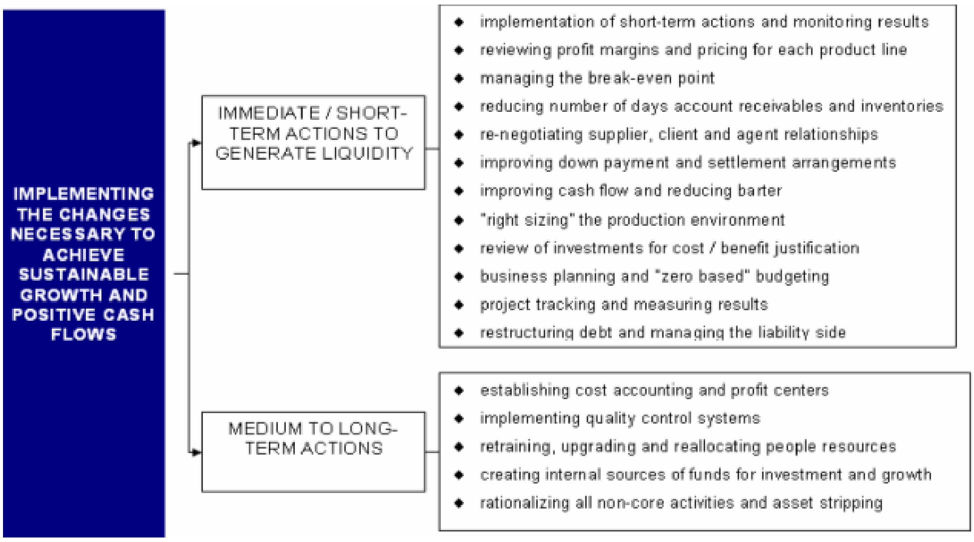

Figure no. 2 Implementing the changes necessary to achieve sustainable growth and positive cash-flows

In order to quickly assess a company, the technique of "Risk Mapping" can be employed.

This is a process of reviewing the operating landscape of a company – its internal operations, as well as the external environment in which the business is conducted – and identifying the high risk “hot spots”. Having this map will assist a manager and his key staff to focus on areas that can be changed without outside intervention or investment in an effort to quickly build momentum toward restructuring.

These immediate areas of attention are intended to be areas of potential cost cutting in order to generate liquidity on a short-term basis.

The hot spots will be the priority items in a "Short-Term Action Plan" and would be the first phase of an overall restructuring program.

The initial benefits of such a short-term action plan in the case of a company that is not yet privatized could be:

1) To empower the management to take harder and longer-term actions;
2) To buy time and resources needed for an overall restructuring program;
3) To promote further "buy-in" to the process by key staff;
4) To position the enterprise for privatization; and
5) To reduce the drag on the national budget pending transfer of ownership.

The following is a matrix of issues that should be reviewed in the "Risk Mapping" process in order to identify areas that require immediate attention. These issues are "tiered" with the "Short-Term Action" items being within Tier 1 and are generally areas that may affect immediately the implementation process and have good potential to generate immediate liquidity improvement**.**

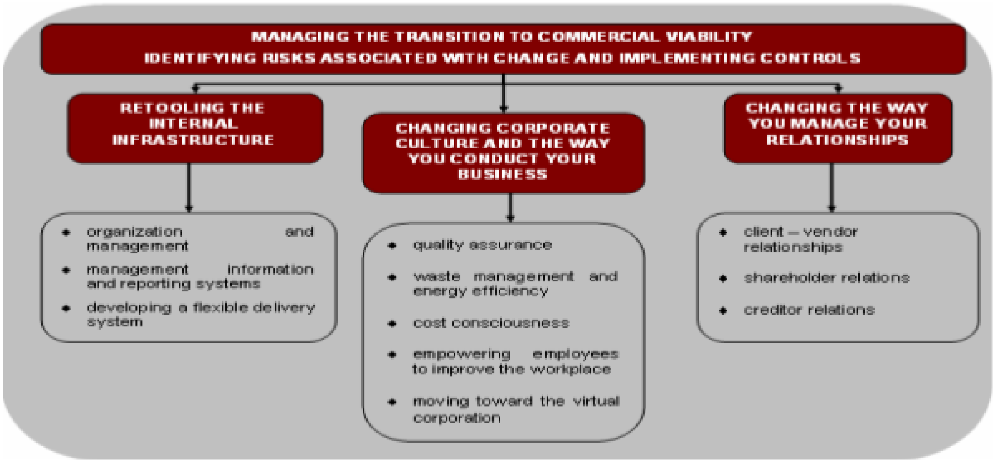

Figure no. 3 Managing transition to commercial viability

5. INSTITUTIONAL LEVEL RESTRUCTURING

Many approaches to restructuring have been utilized in the economic reform era in Romania by different entities – including private consulting groups and government entities – with varying levels of effectiveness.

Restructuring of these large-scale enterprises involves a strategic view and the achievement of financial viability over time.

Any restructuring is made more complex by the overall low level of "commercialization" of these companies. Therefore, the success of this process can only be measured over time and in terms of the ultimate turnaround and privatization of the enterprise.

However, it is also possible to measure near-term "effectiveness" of the process in terms of "incremental benefits" realized by "commercializing the enterprise pending the ultimate transfer of ownership through privatization" – i.e. Pre-privatization Restructuring.

Efficiency-based restructuring is a realistic approach to the restructuring of a large number of complex enterprises across a wide range of industrial and agricultural sectors within a short timeframe and with limited resources. This approach maintains a primary objective to identify immediate improvements that can be incrementally implemented by the enterprise management, with little or no outside intervention, in order to buy the time necessary to achieve overall turnaround of the company.

This incremental process must be measured in new ways and monitored in stages to identify any need for "mid-course corrections" to the approach and methodology being used in the longer-term restructuring of a particular enterprise.

For example, in the case of complex companies, the initial evaluation process can take up to 180 days to complete and obtain the necessary review and approvals from stakeholders.

During this timeframe, the financial condition of that company can improve or deteriorate sufficiently to warrant a graduation to a more or less drastic set of turnaround measures.

Therefore, time is of the essence and it is imperative that immediate steps be taken to prevent further deterioration of a company's operations and to preserve value that can ultimately be privatized.

The basic approach to "Efficiency-Based Restructuring" involves the following:

The selection of the right approach to restructuring each enterprise depends on a number of variables – some of which include:

(a) profile of the enterprise(s) to be restructured, the particular industrial or agricultural sector involved, as well as the capabilities of the entity overseeing the project
- level of distress and risk of survival of the enterprise.
- type and size of enterprise
- number of enterprises and sites involved and other logistical issues.
- level of expertise within the evaluating organization and in the selected enterprise to be restructured.
- importance within the sector of the enterprise and existence of an approved strategy in the sector.
- strategic importance of the enterprise activity (in terms of export earnings, sole producer status, principal regional employer, etc.).
- level of technology installed in the enterprise and the level of integration within the sector.
- attitude of management, unions, line ministries towards the process.

(b) scope of program and resources available
- budget and timeframe available and linkage with schedules for other national programs.
- pre-privatization vs. post-privatization restructuring.
- number and complexity of deliverables required (i.e. short-term action plans to achieve quick liquidity, conciliation agreements and detailed debt workout plans, strategic turnaround programs, environmental assessments, re-deployment schemes).
- availability and integrity of up-to-date financial and operating information on the enterprise(s).
- direct linkage with and mandate to carry out a program to privatize the enterprise.

(c) general environment within which the project is being conducted
- number of stakeholders involved and level of commitment to the process
- mandates from the shareholders (government or private)
- legal framework (i.e. insolvency law passed and mobilized) and legal status of enterprise to be restructured

- level of outside intervention required for technical assistance, periodic reviews and approvals, etc.
- linkage with other national priorities (such as international financial institution programs)
- existence of strategic alliances and cooperative agreements
- life span of entity responsible for restructuring (i.e. task force vs. government agency).

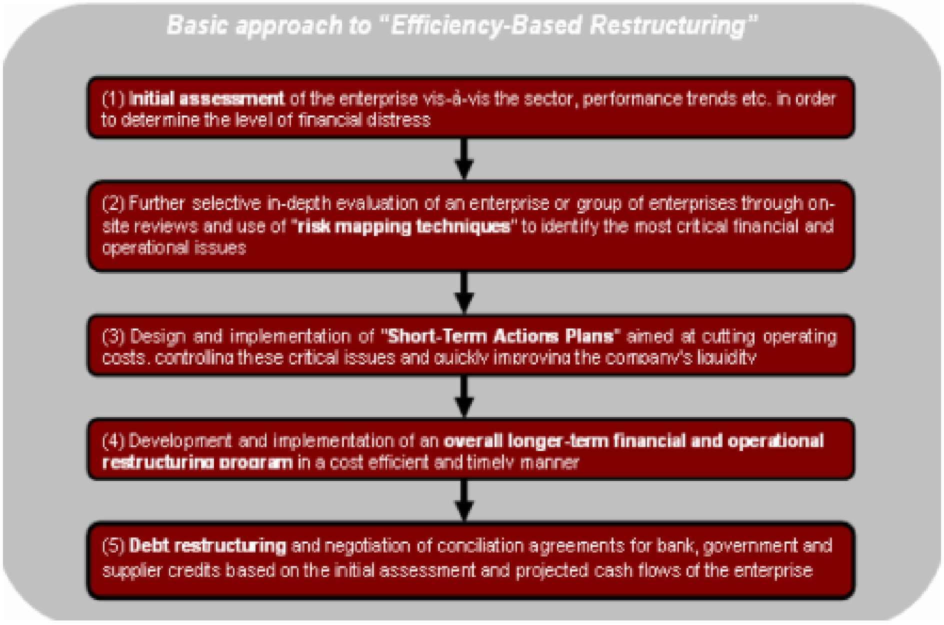

Figure no. 4 Basic approach to Efficiency-Based Restructuring

Compounding the restructuring process in Romania might be a "macro-level controversy" as to whether or not the Government should be involved in restructuring and indeed should restructuring be left to the "new owners" – i.e. Pre- vs. Post-Restructuring.

The "ruling" on this issue by the Government seems to be fairly straight forward – many of the large scale distressed companies in the Government's portfolio, which are also in most cases significant hard currency revenue generators, are considered not privatizable without major restructuring.

In Addition, the Government subscribes to the premise that there are a number of measurable benefits to be realized in "Pre-Privatization Restructuring" which can achieve some of the same overall objectives as privatization.

The following is an overview of the general rationale, stages of production and principal benefits of the "Pre-Privatization Restructuring" approach and outlines the underlying principals behind the Government's activities:

The "Critical Path for Economic Reform" has included initial actions by the government to stabilize the macro-economic situation and prevent further deterioration of commercial value in the country.

With evidence that a degree of macro-economics stability has been achieved, it was important to link this window of opportunity with selective enterprise level initiatives that, once mobilized, could result in further stability across the economy.

Principal objectives and initial benefits of the approach to restructuring prior to privatization will be:

a. identify the obvious liquidation candidates and separate them from other enterprises that appear to have commercial viability over time.
   Also, identify early warnings for stakeholders in order to position for difficult short term actions that might be necessary and that might have significant regional or sectorial impact.
b. allocate scarce national resources more effectively to viable entities on a select basis in order to preserve commercial value and to buy sufficient time for the enterprise to achieve financial turnaround.
c. through financial restructuring, develop more viable and attractive investment targets and thereby achieve best price for the assets.
d. identify potential for rationalizing industrial sectors by means of mergers, acquisitions and spin-offs that result in a stronger, more competitive aggregation of select industrial assets.
e. insure a better rate of survival of the enterprises after privatization.
f. identify operating environments that could be made more efficient and competitive through know-how transfer programs that deliver needed management and operating expertise and techniques and thereby prepare the enterprise management for privatization.

6. UNIQUE APROACH TO THE RESTRUCTURING PROCESS

A) Establish a "Special Designed Delivery System" and a core team of professionals geared to deliver the following products for a wide range of industrial and agricultural activities within an immediate timeframe and with limited resources:
   1. Short-term action plans
   2. Conciliation agreements
   3. Financial restructuring plans

B) Establish a "Partnership for Privatization" with the enterprise through "Cooperative Agreements" that provides for the joint development by the agency and the enterprise management of the above products.

C) Establish "Strategic Alliances" with other entities such as line ministries, multilateral organizations, etc., that share a "Common Purpose" in reforming the economy.

Through these "Special Purpose Alliances", obtain the necessary inputs and critical resources to develop solid turnaround plans for the enterprises and obtain the "bridges" necessary to deliver the plans within a critical timeframe.

Conduct initial evaluations of the enterprises and develop the following:

1. a "Triage" of the involved enterprises and classification of enterprises.

"Early warnings" needed to alert the various stakeholders and allow them to make appropriate interim decisions.

2. Short-term action plans (STAPs) that can be incrementally implemented by the enterprise management to reduce financial overheating during the period the longer term plans are being developed.

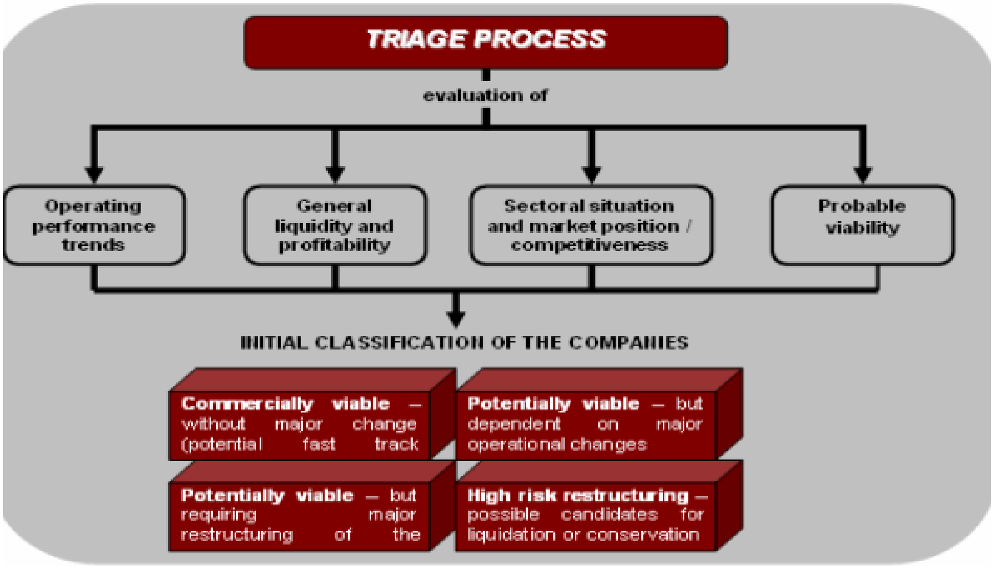

Figure no. 5 Production process – stage 1

3. "Discretionary credit guidelines" (CAP'S) that will provide enterprise specific interim support that is justifiable and which will allow the enterprise to continue operations during the restructuring process.
4. "Special technical assistance" that will put in place immediately needed management and operations expertise and provide key know-how to the enterprises and better position them to manage the transition process and for privatization.
5. proceed with further in-depth operational and financial analysis of the enterprises while closely monitoring the incremental implementation of the STAPs and CAPs and adjusting for "mid-course" improvements or deterioration of the enterprise.
6. carryout an in-depth appraisal of the debt structure of the enterprise and develop initial strategies for obtaining conciliation agreements and "work-out plans" between the enterprise and their creditors.
7. finalize the "financial restructuring plans" (FRPs) and carryout a full review process to include the principal stakeholders and ensure that there is a tacit "Buy-In" agreement among all the parties in order to facilitate the implementation process.

Besides the initial classification of the companies, the triage process also provides with an indication of an appropriate Approach and Methodology for Processing the enterprises.

Stage 1

The "triage process" is important in marking commercially non-viable enterprises and obvious liquidation candidates early on in the evaluation of these distressed enterprises.

This allows for separation from other enterprises that appear to have commercial viability over time and gives an "early warning" to stakeholders in order for them to position for difficult short term actions that may be necessary and that might have significant regional or sectorial impact.

Also, by identifying up front any commercially viable enterprises, better allocation of scarce national resources can be achieved by directing support to these viable entities rather than to liquidation candidates.

Continuing support of the enterprise in this selective manner will preserve commercial value and buy sufficient time for the enterprise to achieve financial turnaround.

Stage 2

The next stage of activity involves an in-depth evaluation of the operations and finances, as the foundation for developing comprehensive restructuring programs that will result in better survival rates of these companies after privatization

In addition, an in-depth "Due Diligence" prior to privatization can result in higher levels of commercialization and improved performance in these enterprises thereby making them more attractive investment targets and achieving better prices for the assets.

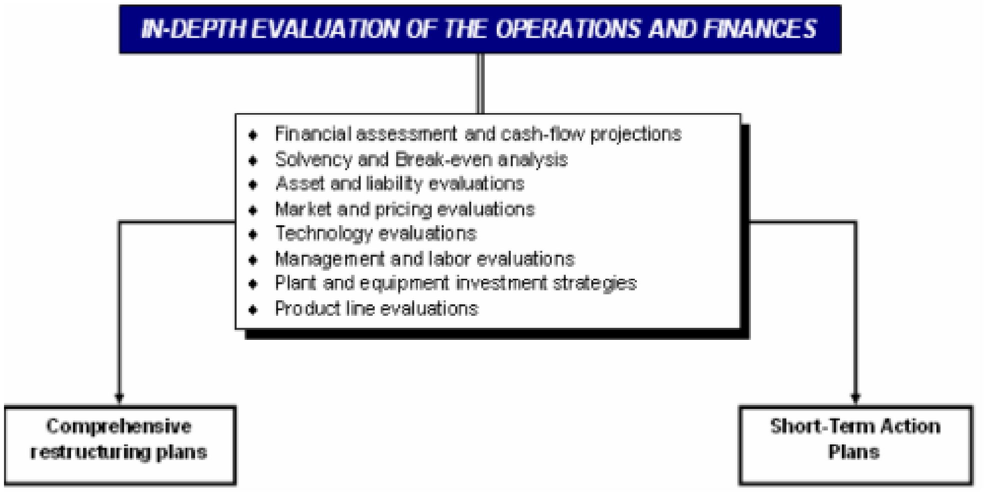

Figure no. 6 In-depth evaluation of the operations and finances

While the Comprehensive Restructuring plans are being developed (90-120 days), Short-Term Actions are identified very quickly that can be incrementally implemented to cut operating costs and generate better cash flows in the interim.

These actions involve straightforward changes such as energy utilization controls and waste minimization programs that do not require outside intervention.

The evaluation process is carried out on-site at the enterprise and is closely coordinated with the related line ministry. This process involves the assessment of every major element of the company's operations among which are:

⇒ Financial assessment and cash flow projections
⇒ Solvency and Break-even analysis
⇒ Asset and liability evaluations
⇒ Market and pricing evaluations
⇒ Technology evaluations
⇒ Management and labor evaluations
⇒ Plant and equipment investment strategies
⇒ Product line evaluations

Stage 3

After the “in-depth” evaluation of the company's operations and financial situation has been done, there is the ability to identify potential for rationalizing industrial sectors through mergers and spin-offs. This of course results in a stronger, more competitive aggregation of remaining industrial assets.

Throughout the process, specific efforts are made to transfer know-how to the enterprise management and deploy operational enhancements into the production environments.

This all leads to improved rates of survival after privatization.

Additionally, by working closely with the enterprise management, increases the ability to identify operating environments that could be made more efficient and competitive through further special technical assistance programs designed to download vital management and operating expertise which serves to prepare the enterprise and its management for privatization.

As by-products of the process, special purpose Valuations provide the enterprise and stakeholders with special benefits such as:

1. An Environmental Valuation to identify potential issues that would create an obstacle to privatization or that would represent significant financial risks to the future operations of the enterprise.
2. A Re-deployment Valuation that outlines schemes to assist the enterprise in dealing with significant downsizing.
3. A Debt Valuation that provides a strategy for conciliating the outstanding debt and arrears of the company through write-offs, debt holidays, rate concessions and/or debt equity swaps.

Stage 4

The final stage in Pre-Privatization Restructuring is to identify specific linkages to privatization where possible and identify "Post Restructuring" Assistance Requirements that addresses on-going needs of these enterprises and continue the "Commercialization" of the enterprise pending privatization.

Continued Technical Assistance in upgrading the production, management and marketing capabilities and that integrates with and enhances the know-how initiatives during the process of developing financial restructuring plans.

Development of capital plans in line with the enterprises restructuring plans and access to reasonably priced working capital through special credit support and guarantees in sync with the changing working capital needs of the enterprises that demonstrate positive turnarounds in their operations.

Ongoing assistance and follow through on merger and acquisition opportunities, phased right-sizing through spin-offs and production rationalization plans and conservation or liquidation programs.

7. COST EFFECTIVE RESTRUCTURING

With an expanding portfolio and delivery time frames constricting, it will be necessary to find ways to be more efficient in the way is carried out its incremental projects.

Following on this efficiency theme, a number of other "Efficiency-Based" techniques and methodologies have to be developed and employed – namely:

a) "Triaging" of the Portfolio – i.e. quickly assessing the level of financial distress and survivability of the enterprise and allocating resources accordingly;

b) "Fast Tracking" through the process any "quickly privatizable" enterprises or enterprises that are clear cut liquidations situations;
c) "Risk Mapping" the operational landscape of an enterprise (i.e. isolating high risk areas of an operation) and "Early Warning" advisories issued to various stakeholders such as the Ministry of Labor in order to position for significant downsizing in a particular enterprise.
d) Short-Term Action Plans (STAPs) that focus on near-term liquidity (reducing the number of days inventory and account receivables, asset stripping and downsizing, etc.) which are incremental implementation by enterprise management while simultaneously developing a full-scale turnaround program.
e) Enterprise by Enterprise vs. Sector Restructuring (i.e. focus on top 2 or 3 sector leaders with the majority of market share). By restructuring these major market share companies, certain forces within the sector will be generated and will drag peripheral operators and suppliers into the process.
f) Develop Generic Models for rapid deployment in low risk enterprises with standardized operations.

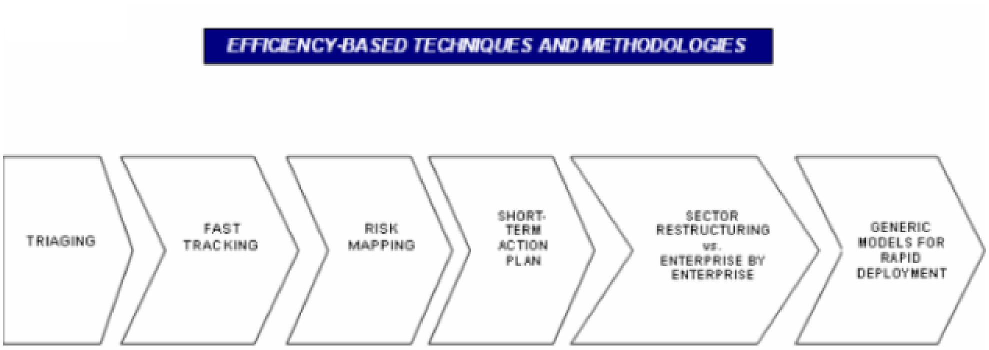

Figure no. 7 Efficiency-based techniques and methodologies

g) Downsizing of staff is a key indicator of the general willingness of enterprise managers to build momentum in turning around their operations and to demonstrate a firm position on restructuring in general.

8. CONCLUSIONS

Restructuring is most certainly a process that requires continuous monitoring. This is critically important for the following reasons:

a) By restructuring the largest operations in an industrial sector, there is the opportunity to rationalize that particular sector – likewise, deterioration of the financial condition of these enterprises will impact on the competitiveness of the sector overall;
b) The success or failure of this activity will be a prime signal to investors – both domestically and off-shore;
c) There are scarce national resources for development and growth of the private sector. Successful restructuring of State-Owned enterprises – whether privatized or not will

reduce the drag on the national budget and allow for more efficient allocation of resources.

d) With the debt of some of the large loss-making enterprises having been restructured, it will be important that these enterprises are not back at the table so to speak. Their performance in line with the projections of the restructuring plans and return to a current debt servicing status will certainly assist the restructuring of the banking sector as well.

It will be very important not to simply put these enterprises onto a program of what in many cases will involve complex and high risk changes without paying attention to their needs for expertise. Therefore, specialized technical assistance may be necessary in the are-as of cost accounting, energy management, quality assurance, marketing and capital planning.

Also, many of these enterprises, having just undergone what is essentially a "Pre-acquisition Due Diligence" and having significant parts of their debt written down or re-scheduled are now in a prime position to attract new capital. Therefore, management of these companies could benefit from assistance in structuring an investment proposal as well as soliciting and negotiating offers.

The "Pre-Privatization" process is designed to define the strengths and weaknesses of the enterprise, put in place a program to enhance the strengths and minimize the weaknesses – simply, the process identifies the risks and clarifies to some extent the value and with this a "price" can be developed for negotiation with potential investors. Not knowing the value and risk associated with an enterprise are the single biggest obstacles to privatization.

It will also be necessary to develop a real capability within the enterprises to monitor their own operations and build a meaningful "Decision Support System" out of their own data bases.

There is the possibility that the same management practices which evolved from the previous central planned economy will make it difficult for companies to take the initiative in monitoring, evaluating and pro-acting relative to their own operations.

Likewise, in attracting new capital there needs to be the legal framework and available expertise for innovative tools such as Asset Drop Downs, leasing of production assets with options to buy, professional valuation infrastructures and hybrid debt and equity instruments (i.e. convertible debt, preferred shares, etc.)

Special skills and services will need to evolve to deal with emerging needs of these companies – particularly in the area of:

- Energy management and waste minimization;
- Environmental audits and pre-acquisition due diligence; and
- Quality controls and certifications.

Overcoming the issues on legal framework and overhanging government regulations will require the amalgamated lobbying and expertise of all the stakeholders.

Also, innovative alternatives to privatization need to be explored. It is clear that privat-ization will take time for many of the larger enterprises, and in the interim, concepts such as National Clearing House for idle production assets and liquidation assets as well as other forms of special purpose consignments could be useful in effectively reducing the holdings and involvement of the state in enterprise operations.

Possibly the most important issues related to successful economic reform and selective restructuring are:

I. Management of the process – it is critical that a properly mandated entity with sufficient resources be at the helm – a special purpose "task force" oriented approach is needed to draw together all of the key elements and mobilize a practical program.
II. Measurement of success – there are controversial aspects of this activity and there will be a search for failure and a search for success on the opposite poles of the issue. Therefore, it is critical that credible and timely indicators be provided to all stakeholders – chief among these are the managers of the enterprises themselves. They must be able to measure success at the enterprise level and use this as a decision support mechanism as well as a tool for competing for resources.
III. The "Demonstration Effect" – this is important to achieve "buy-in" within and outside the enterprise – in short nothing can sell the concept of "Pre-Privatization Restructuring" better than being able to clearly measure success.

This can be done by acknowledging that improved liquidity, real growth of hard currency revenue streams, and cutting energy costs in a sustainable way are a more important measure of successful commercialization than the number of staff that has been downsized.

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