

## 2. Turning around struggling state-owned enterprises in developing countries: The case of NWSC-Uganda

### Abstract



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*The conventional thinking has, hitherto, been that state-owned enterprises cannot perform well and should be restructured with a view of privatising them or at least putting them under private sector management. In this paper we outline how NWSC, a state-owned water corporation in Uganda has internally restructured itself and improved performance significantly from 1998-2006. We discuss the key managerial approaches and success factors. We also outline the role of the private sector and observe that 'international operators' do not come to manage problems but to earn returns on their investments. We also note that donors still need to play an important role in the restructuring of state-owned enterprises but that such collaboration must be executed in a meaningful manner, encouraging a 'do it yourself policy' for the process owners. African proverbs are interspersed throughout the article to underscore key themes.*

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## Introduction

**“ A person, who never travels, believes his mother’s cooking is the best in the world. ”**

**- Kiganda, Africa, Proverb**

The National Water and Sewerage Corporation (NWSC) was established in 1972 and is wholly owned by the Ugandan government. The corporation is mandated to operate on a commercially viable basis and to manage the water and sewerage service in 22 urban towns.

In 1998 NWSC was not a healthy organisation. The World Bank noted: “Over the last 10 years, the Government of Uganda, in partnership with the World Bank and other Donors, has made a significant investment (over US\$100 million) in the urban water and sewerage sector. These investments have contributed immensely in rehabilitating the existing infrastructure under the NWSC management. Unfortunately, these investments have not been matched with the necessary efficient commercial and financial management capacity that can ensure the delivery of sustainable services in the medium to long-term.”<sup>9</sup>

This conclusion, based on a thorough analysis, found that the corporation had sound infrastructure, abundant water resources, and enabling legislative framework. However, the corporation had a large and inefficient labour force with conflicting and overlapping roles, high unaccounted for water (more than 50 per cent), poor customer service, low collection efficiency (about 71 per cent), substantial accounts receivables (days receivable ratio of about 420 days) and corruption within the work force, especially field staff. There was a running monthly deficit of about Ushs348

million (US\$300,000) despite a high average tariff of Ush1100/m<sup>3</sup> (US\$1.00/m<sup>3</sup>). In other words NWSC was in a near state of bankruptcy.

Apart from the weaknesses, the corporation had to contend with a number of threats, including debt servicing obligations coming due and a VAT law that compelled NWSC to pay taxes on any increases in bills. On the other hand, the government was willing to give support to pro-active managers and the economy was relatively stable. In this respect, the government was willing to freeze the debt (US\$100 million) for some time to give a chance to the corporation to recover, if serious managerial efforts were initiated. Overall, improving operational and financial performance was essential to prevent further deterioration.

This paper outlines the corrective actions undertaken by NWSC management and staff to turn around performance,<sup>10</sup> the sequence of those steps and the outcome of the reform programme. The paper demonstrates to managers of poor-performing utilities the benefits of new initiatives. Such initiatives are not painless, nor can they guarantee success. However, citizens and political leaders are finding the status quo unacceptable: organisational transformation based on feasible commercial plans and team initiatives can improve performance.





A woman accesses clean water in a communal yard

## Initiatives undertaken to turn around performance

**“ The hunter in pursuit of an elephant does not stop to throw stones at birds. ”**

**- Ugandan Proverb**

Staying focused is crucial. In an effort to address managerial inefficiencies in NWSC, the government appointed a new Board of Directors. The new Board comprised representatives from local governments, the business community, professional bodies, environment, and Ministries of Finance, Water, Health and Small Scale Industries. The composition and structure of the Board enabled

it to exercise its governance functions properly and was able to shield the corporation from political interference and patronage.

The new Board, in turn appointed a new Managing Director, Dr William Muhairwe,\* who was given the mandate to re-think strategies for performance improvement.<sup>11</sup> The appointment led to an emphasis on commercial viability, with ‘customer care’ as a theme. The Board and new management also arranged performance contracts with government where roles and obligations were clearly spelled out.

\* Dr. William T. Muhairwe is a Management Specialist trained in Economic and Business Management and has been managing public companies for the last 15 years in Uganda and abroad. Formerly, Dr Muhairwe worked for the Uganda Investment Authority as its Deputy and eventually Acting Executive Director for 3 years and was responsible for attracting inward private investments to Uganda. He was also, at one time, the MD of the East African Steel Corporation, a Joint Venture Company between the government of Uganda and a private company (The Madhvani Group).

Fortunately for the new team, everyone was aware that the ship would 'sink' if nothing was done to remedy the situation. Dr. Muhairwe decided to adopt the approach of working with everybody, despite origin and colour. And it was the incumbent staff who initiated the programme of change.

At the tactical level, the new Board and management came up with a series of programmes: reversing operational and financial inefficiencies, restoring customer confidence and achieving commercial sustainability.

The Corporation had to improve operating margins by reducing bureaucracy, increasing staff productivity, and encouraging worker involvement. By working with the unions, management was able to reduce excess staff by half from 1,800 in 1999 to 900 in 2001, without any industrial unrest. The tactical programmes were designed to improve moral and alter the expectations of operating staff. Organisational change was accomplished through two other initiatives that reduced the stress of the hierarchy and also encouraged individual performance accountability.

### 1. Internally-Delegated Area Management

**Contracts** give more autonomy to Area Managers (Partners),\* defining roles and responsibilities more clearly, and creating better incentive plans that allocate more operating risks to Partners.

**2. External Services Unit** – No organisation can be successful in isolation: collaborations allow managers to learn about the strengths and weaknesses of peer companies. Through this Unit, the Corporation has established a mechanism for sharing experiences and rendering consultancy services to outside companies, on a cost-covering basis.

\* Under the IDAMCs, the Head Office enters into an internal non-legalistic contractual arrangement with Partners in Areas. The Partners are a team of senior managers in the Areas/Water utilities, who are bound together by a Partnership Deed detailing how business shall be conducted during the period of the internal contract. The Partners are headed by a Lead Partner, who is the accounting officer of the water utility/Area.

One factor supporting the favourable outcome to date is the performance contract between NWSC and the government of Uganda represented by the Ministry of Water and Ministry of Finance. The targets and reporting procedures have institutionalized accountability, without introducing a separate agency to monitor the firm. At some point, current arrangements will come under review. However, the arrangements have been beneficial to date, in contrast to patterns observed elsewhere. It may be that the second generation of performance contracts have benefited from the experiences of others.

## Main performance considerations

“Between imitation and envy, imitation is better.”

- Ekonda Proverb, Democratic Republic of Congo

NWSC performance improvement programmes are both internal and external.

**Internally**, NWSC developed a programme design outlining clear roles and responsibilities; bottom-up approaches to strengthen programme ownership and support and SMART (Specific, Measurable, Achievable, Realistic and Timely) targets that were later strengthened through use of 'stretched' (tougher) targets. Managers were forced into competition as well, preventing staff already in place becoming stale.

The other major incentive was the threat of privatisation from government and donors. The managers and staff were aware that there were many potential substitutes outside who would take over if NWSC improvements were not forthcoming.

**Externally**, the corporation enjoyed significant government support, which resulted in a debt freeze and non-interference with the corporation's management. Being somewhat

insulated from political pressures meant that managers could focus on commercial issues in the early years of reform. At the same time, donor support in the form of financial and technical assistance added to the capabilities of the organisation.

Customer and public confidence in NWSC performance improvement initiatives turned out to be another external factor that motivated staff to innovate further. NWSC's turn-around was good news, and captured media headlines. Pride based on genuine accomplishments gave confidence to mid-level managers that they were on the right track.

## Accomplishments and challenges (1998-2006)

**“ A forest cannot be cut with a broken axe. ”**

**- Bantandu Proverb**

The reform initiatives from 1998 – 2006 have had positive impacts (see Table 1 below).

Positive cash flows have financed network expansion and enabled maintenance programs to be scheduled and implemented.

Despite the accomplishments, NWSC still faces challenges in the area of sewerage where the coverage is about 10 per cent. The sewerage investment costs are inherently very high and the Corporation is currently finding it hard to devote resources to such investments. Therefore, achieving the Millennium Development Goals remains a distant goal.

NWSC also faces the challenge of serving the poor communities where cost recovery is questionable. The infrastructure in such communities is very poorly planned and extending services to such areas involves significant difficulties. Nevertheless, the organisation continues to explore cost-effective ways to carry out this task.

The original approach to service for the poor in NWSC was through use of water kiosks/communal taps. However, through experience, it has been found out that the water vendors at these points sell water to the users at a price 4-8 times that offered by NWSC. This 'middle-man' effect defeats the whole objective for which the pro-poor tariff was set. It affects

**Table 1. Improvements in NWSC performance 1998-2006**

	<b>1998</b>	<b>2006</b>
<b>Service coverage</b>	48%	70%
<b>Network coverage</b>		<b>Increased by 52%</b>
<b>New connections per year</b>	3,317	23,312
<b>Total connections</b>	50,826	148,312
<b>Unaccounted water</b>	51%	29%
<b>Proportion metered accounts</b>	65%	99.6%
<b>Annual turnover</b>	US\$11 million	US\$34 million
<b>Profit</b>	US\$0.4 million loss	US\$34 million surplus

the willingness and ability to pay and restricts consumption thereby obstructing health enhancement initiatives. In order to address this service problem, NWSC has come up with a *new connection policy*, which aims to subsidize access and charge consumption at affordable rates. The policy also incorporates network intensification in the poor communities in order to reduce connections lengths to individual households. Consequently, each household in the poor community areas is encouraged to connect a yard tap and pay directly to NWSC. This approach is working very well, so far.

### Monitoring technical processes and inputs

**“If you want someone more knowledgeable than yourself to identify a bird, you do not first remove the feathers.”**

**- African Proverb**

Withholding information reduces the likelihood that problems will be correctly identified. In NWSC, the Head Office has established a monthly magazine called the *Water Herald*. This magazine allows utility managers to describe their innovations, identify binding constraints and receive credit for achieving targets. The magazine captures the ‘dos’ and ‘don’ts’ experienced in the previous month, outlining how peers can copy and adapt good practices and avoid pitfalls. The magazine also displays a monthly performance scorecard detailing the relative performances on key criteria and how much incentive awards were earned by staff and water utility management. Incentives

can involve bonuses of up to 50 per cent of salaries.\*

The Head Office also established a ‘checkers’ system in May 2005. Performance criteria are agreed upon and compliance is checked on an unannounced basis. Consistent failure may mean that managers of water utilities lose their jobs and/or responsibilities because of breach of internal contracting obligations.

### Monitoring customer protection processes

**“A family is like a forest; when you are outside it is dense, when you are inside you see that each tree has its place.”**

**- Akan, Ghana**

Water and sanitation are prerequisites of human well-being and crucial ingredients of sustainable economic development. As a result, because of the technical difficulties involved in introducing meaningful *in-market* competition, services have remained largely monopolistic. NWSC has utilised a number of approaches to track customer perceptions/complaints; subsequent incentives are directed at helping managers achieve ‘customer delight’ over services.

There are two major approaches used in NWSC to capture customer complaints and compliments. The first process involves capturing formal customer complaints. And the second mechanism is routine customer satisfaction surveys.

\*NWSC salary structured is determined by the Board of Directors and is generally competitive among Ugandan companies (public and private). Coupled with incentive payments, this partly explains why staff are motivated and committed to continuous improvements.

The annual average proportion of customers satisfied with NWSC's service quality has improved from 70-75 per cent in 2000 to 85-90 per cent in 2006. The main service quality aspects, which are routinely surveyed, include pressure at the taps, quality of water, and accuracy of bills, reliability and customer handling by interfacing staff. Inadequacies and shortfalls are routinely identified and used as weaknesses to be addressed in subsequent performance improvement efforts.

### Putting emphasis on what works: The right mindset matters

**“ Do not throw away  
the oars before the  
boat reaches the shore.”**

**- Mpongue Proverb**

The successful implementation of the performance enhancement initiatives across NWSC's operating units suggests that the conventional wisdom regarding non-performance by public companies is incorrect. The NWSC experience clearly shows the benefits of focusing on what works. There is no single textbook solution to the myriad problems facing water utilities, especially in low income countries. Most of these problems are caused by the local managers, poor organisational cultures, citizen non-payments, and political intrusiveness.

Conventional thinking reflects the view that managerial practices under public management settings are fundamentally flawed, reflecting frustration with poor performance of public companies. Nations often become trapped in a 'low level equilibrium' involving low prices, low quality, slow network expansion, operating inefficiencies, and corruption. The situation is 'stable' in a sense as managers pretend

to manage, their utilities pretend to deliver services, and customers pretend to pay.

When an inefficient water utility lacks cash flow, Treasury funding dries up. This can lead to 'desperate solutions': privatisation. However, an independent consultant for NWSC remarked, "governments should never expect to privatise their problems to international companies and think it will work".<sup>12</sup>

Indeed, the private sector participation experience at NWSC suggests that 'international operators' do not come to manage problems but to earn returns on their investments. They leave the country if their profits slacken.

International operators do not have a monopoly on approaches to improving performance. From NWSC's experience, excellent performance can be 'home-grown', but such an outcome requires a set of conditions. Strong leadership, the right tools (legal framework), appropriate skills, and a clear set of shared objectives. Nevertheless, one wonders why have so few water utilities been reformed and transformed? Current managers have knowledge and skills, but they often lack the incentives to make the extra effort and make some difficult decisions. For many utilities, local managers, are the starting points for improvements in performance.

External opinion should be treated with caution. In some cases consultants actually over-estimate institutional problems, or underestimate the capabilities of state-owned enterprises. Their actual intentions may not be consistent with public statements, as some of them seek investment opportunities for the firms they champion.

Other stakeholders represent international banks, which support the 'policy flavour of the month'. While both groups can provide capital through a variety of arrangements, they can prematurely damage initiatives that the company is planning and/or implementing. Conditionality becomes another word for 'policy being dictated by those who are unfamiliar with issues' on (and under) the ground.

Communicating with such groups, and convincing their representatives that the local team can succeed, requires a substantial investment of time. That investment is necessary. In some cases, the dialogue leads to better plans; in others, the local team is able to persuade these important stakeholders that the highest payoff will come through local talent, insulated from volatile political forces. As NWSC entered the process, managers realized that they needed to identify their roadmap, accept constructive advice, respect differences of opinion, and ensure that company values and objectives were at the centre of everything. International consultants have a role in the process, but the ultimate decisions cannot be delegated to professionals who lack a deep understanding of national institutional constraints and unique local opportunities.

### Matching performance improvement initiatives to prevailing conditions

**“ The new moon can not come out until the other has gone. ”**

**- Bahunde or Hunde Proverb, Democratic Republic of Congo**

The cycle of poor performance in most utility companies in developing countries has often resulted from inadequate cash generation, which in turn affects payment of staff salaries, basic infrastructure maintenance, network expansion and consequently, employee moral. Without a sense of team spirit and clear managerial objectives the system becomes dysfunctional.

Management is crucial at this stage. Performance targets must be set and incorporate high-impact financial improvement indicators such as cash collections. Once the financial operating

efficiency of the company improves, the accruing efficiency gains will help to alleviate cash-flow problems. This also aids morale.

Once the teams have been consolidated and financial operating efficiency improved, the company can move into more complex internal contracting arrangements incorporating both individual and group commitments. The individual contracting element strengthens individual performance accountability within a team and ensures equity in handling workloads.

### Managing organisational rigidities and inflexibilities

**“ If the rhythm of the beat changes, the dance step must adapt. ”**

**- Swahili Proverb, East Africa**

Managers in bureaucracy-ridden utilities in low income countries can easily become prisoners: constructing the very bars that hold back good performance. Pretending there is no problem is a natural response: those bureaucratic procedures may once have had justifications. However, the cumulative effect of rules, strict hierarchical reporting systems, and committee approvals imprison initiative and destroy ideas for improving performance. The leadership at NWSC has insisted that managers *'break all rules and procedures'* that do not make sense and which are, therefore, roadblocks to innovation. They are urged to put performance and service delivery to the forefront.

Favouritism, tribalism and nepotism, must be addressed head on, since these are common governance problems in developing countries. It leads to bias in managerial decisions and in most cases demotivates the staff. Managers must earn the trust of colleagues, achieved through high performance, authenticity and transparency in all that is done.





Laying of new pipes by NWSC

## Realities about moving towards cost recovery frontier

**“ If you refuse the elder’s advice, you will walk the whole day. ”**

**- Ngoreme, Tanzania**

Perhaps the most difficult managerial task in developing countries, after turning the organisation around, involves moving towards full cost recovery. This is seen as a ‘rigid’ position taken by some donors, who argue that water companies must reach this stage as soon as possible. The NWSC experience has shown that premature price increases ultimately choke off reform within water companies.

First of all, the cost-recovery idea is good but politically unachievable in the short to medium term, especially in developing countries. Reaching this frontier requires significant tariff increases (doubling, tripling and sometimes quadrupling). Tariff increases require a thorough structured analysis of citizens’ willingness and ability to pay. We know that water that is trucked to peri-urban areas is much more expensive than piped water, but citizens already receiving service will revolt against substantial price increases.

In developing countries, especially in Africa, economies are still evolving and cannot support huge tariff adjustments. Such actions would lead to customer anger and civil disobedience. This would, in turn, have negative effects on the company’s ability to collect bills, leading to poor cash flows. Such actions disrupt network expansion and severely compromise the company’s ability to equitably distribute water supply services to the citizens of the country.

On the other hand, price freezes do not make sense either. NWSC experience has demonstrated

that there are benefits from following an *incrementalist approach*, indexing the tariff nominally against inflation, foreign exchange and key input price changes. This long term approach takes the tariff to cost-covering levels without causing undue agitation and unrest.

Of course, care must be taken that such tariff changes are not used to finance managerial inefficiencies. Managers should not be in the habit of thinking ‘every time there are cash-flow problems, we should increase tariffs’.

This suggestion means that the issue of full cost recovery should be tackled in a phased manner. Big investments like treatment plants, transmission mains and big network systems cannot easily be financed through revenues generated from tariffs. These can be financed through grants from development partners or government subsidies. However, such grants must be properly targeted and implemented in an efficient manner.

## The role of donors

**“ Water that has been begged for does not quench the thirst. ”**

**- Soga, Uganda**

There is evidence that NWSC is on the right track to meet its operational costs, but the delivery of water and sewerage services is too expensive for NWSC to handle by itself. Therefore, the corporation will continue to request donor support for its long-term capital development projects in order to improve its services to the rapidly growing urban population. The corporation has earned credibility through its performance. Donor confidence and support have led to increased long term capital investments being incorporated in the Medium Term Expenditure

Framework financed by government and donors. If the present momentum of NWSC-donor collaboration continues, the prospects are good for continued reform and, ultimately, the creation of a viable commercial enterprise.

## Concluding remarks

**“ There are forty kinds of lunacy, but only one kind of common sense.”**

**- African Proverb**

The lessons from the NWSC experience show the value of experimentation and decentralization without losing contact with experts at the centre.

A hard working and committed Board of Directors is necessary if an organisation is to make progress. In addition, a dynamic utility management and staff team motivated by clear vision, mission and objectives is fundamental to success and necessary to secure government and donor commitment to support key initiatives.

Monitoring both technical processes and customer relations is very important in water utility management. It requires prompt responses, managerial discipline, reasonable flexibility, and understanding on the part of the monitor. A customer complaint does not always mean that the operator is underperforming. It is the *speed of response* and minimisation of repeat complaints that determine the operator's efficiency. On the other hand, monitoring of technical production processes must not interfere with the operator's decision making portfolio. Micro-management is likely to significantly hamper managerial innovation.

Outsourcing is not a panacea. While it can be a good means in itself, it must be well conceived and instituted at a time when the clientele managers themselves feel that they can manage

but simply have peak workloads that make them less productive. If outsourcing occurs because local managers are inadequate, the problem will not go away. The utility is better trying a 'we can do it ourselves' approach.

There is a need to diagnose the company's performance. If the financial performance and teamwork among managers and staff is low, leader/managers need to start with simple performance improvement programmes, incorporating tailor-made incentive plans and targets. In tandem, the teams need to be coached and developed to improve performance. It is from this point that the company can progressively move into more complex internal contracting arrangements incorporating individual and group commitment plans.

While implementing these performance improvement plans, managers ought to know how to deal with internal managerial rigidities and inflexibilities that hamper performance. These can be potential performance barriers if the managers do not have the self confidence to 'demolish' them wherever they do not make sense.

Finally, realities about moving towards the cost recovery frontier need to be addressed. There are not many water companies that can easily attain this performance level in developing countries. The movement towards such frontier needs to be sequenced to minimize adverse effects on the citizens. Targeted subsidies and grants can be used to fill financing gaps, while moving towards cost recovery.

