

## DEVELOPING STATE TRADING IN A PERIPHERAL ECONOMY:

Reflections on Tanzanian Experience Related to  
Papua-New Guinean Possibilities

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The emergence of state trading involves a change in industrial organisation, often involving a change in the nationality of the firms and, a shift from public to private firms. Changes in economic results or in political dynamics will result from an interplay of these three elements. ... the structure of industry establishes the logic of choice and perhaps of action, but not the outcome. The exercise of power determines the outcome, and sufficient power may alter the structure. ... It may be more important to know the nationality of a company than whether it is public or private.

- J. Zysman, "The State As Trader", International Affairs, 1978.

Ideological differences between countries affect the method, not necessarily the fact, of securing national control. The real ideological choice is between controlling the economy through domestic private enterprise, or doing so through some state or other collective mechanism. But ... it is extremely doubtful whether it is a practical choice for an African nationalist. The pragmatist in Africa ... will find that the choice is between foreign private ownership on the one hand and local collective ownership on the other ... A capitalist economy means a foreign dominated economy... The only way in which national control of the economy can be achieved is through the economic institutions of socialism.

- President Julius K. Nyerere, "Economic Nationalism", 1968

I

A. Introduction

This paper seeks to survey the experience of developing state trading (state commercial sector) in one peripheral economy, the United Republic of Tanzania (or more precisely mainland Tanzania), with a view to providing a backdrop and isolating issues for consideration by those responsible for analyzing and advising on the possible development of a state commercial sector in another peripheral economy, Papua-New Guinea.

It does not purport to:

- a. provide a complete, detailed history of Tanzanian state trading, nationalisation or public enterprise development;
- b. present the general theory of state trading (assuming there is an agreed body of theory) especially not in relation to industrial (capitalist or socialist) or medium productive force level economies;
- c. outline a detailed course of action for Papua-New Guinea as opposed to a series of questions, comments and indications of probable choices open and constraints present which may help Papua-New Guinean decision taking. The author has never been to PNG and has no claim to more than a rather cursory and fragmentary knowledge of its specific political, institutional and personnel goals, challenges and constraints.

Tanzanian state trading development over 1961-1978 is examined neither to construct a transferrable model nor to "prove" what PNG decision takers and managers should do or avoid. Reality is more complex than that. The validity of Technical Cooperation Among Developing Countries indeed rests in part on greater similarity of contexts and objectives, but not on any possibility of one to one copying which is almost as unsound in TCDC as in standard Technical Assistance. Nor is it useful to see Tanzania as "an experiment" - no major exercise is an experiment to those who participate in it. To view it as such loses much of its human reality and therefore much of its usefulness to advisers, decision takers and managers seeking to learn from it. However, it is examined to raise questions and illuminate issues likely to be relevant in the context of PNG:

- a. the interaction of freedom (what can be accomplished or what goals could be chosen) and necessity (goals which it was critical to pursue or external realities which had to be faced) and their evolution over time and as a consequence of previous decisions;
- b. the interaction of goals and contexts over time and the way in which they changed as a result both of Tanzanian action and of events beyond Tanzanian control;
- c. the interaction of state trading narrowly defined with other issues - notably price determination, foreign exchange allocation, public enterprise planning and control;

- d. the experience over time with state trading in a political economic context with certain marked and additional more general similarities to PNG at independence.

An attempt will be made to identify the importance of goals for state trading (e.g. national control over the economy, public sector surplus, price control, foreign exchange saving), of particular contexts (e.g. nature of pre-existing private enterprises, characteristics of goods and of purchasers, personnel and institutional capacity available to the state) and of selections made (e.g. sectoral coverage, institutional form, use of external personnel). These will then be presented schematically with more specific reference to PNG. Finally some tentative suggestions as to possible approaches to the development of state trading in PNG will be made.

## II

### B. 1961 - The Starting Point

State trading in Tanzania arose out of the interaction of the colonial commercial context and the goals of the leaders and Party of the newly independent state.

At independence in December 1961 the commercial sector was virtually 100% private. State enterprise - well beyond traditional public utilities but collected on a

rather random basis - was substantial in mining and manufacturing but not in commerce. The bulk of consumer goods import trade was handled by less than a dozen European based firms and the rest by smaller firms owned by non-citizens or members of economically privileged minority communities. Specialist importing was either carried out by specialist European firms (e.g. vehicles, machinery) or was ancilliary to the operations of European owned enterprises (e.g. petroleum). Exports were largely handled by European based merchant or brokerage firms even when nominally state boards were involved. Diamonds were sold by a 50-50 joint venture (Williamsons) to the Central Selling Organisation (De Beers) under a contract whose later amendment suggests that as of 1961 it was quite unfavourable to Tanzania. Wholesale trade was partly by importers, but the majority of it was carried out by perhaps 2,000 local firms - 90% plus owned by non-citizens or members of privileged minority communities. Specialist retailing (e.g. automobiles, machinery, petroleum products) was by importers, the bulk of general retailing was handled by perhaps 25,000 small enterprises (including the smaller wholesalers) again with at least 90% owned by non-citizens or privileged minority community citizens. Co-operatives, while significant in agricultural marketing, were limited in numbers and success in retail trade and non-existent at wholesale and import/export levels.

Because the colonial economy in Tanzania dominantly produced for sale what it did not consume and consumed purchased goods it did not produce, commerce was centered on the import/export nexus with retail and wholesale funnelling to, or channeling out from, the ports. Under a fifth of locally consumed manufactured goods and almost no locally used intermediate or capital goods were domestically produced. In the cases of three exceptions - cigarettes, beer, to a degree cotton cloth - European firm owned factories carried out the wholesale function delivering direct to subwholesalers/large retailers.

Trade in domestic foodstuffs and a limited range of handicrafts were exceptions to the external trade/foreign firm character of commerce. Village markets sellers and town stallholders and "hawkers" were African. In total they did a good deal of business but each seller was economically minute and few had succeeded in advancing to the small retailer with premises rung of the commercial hierarchy. Further, lack of data meant that the size, scope and possible potential of this sub-sector was consistently overlooked or underrated up to the late 1960's, while thereafter the commitment to a transition to socialism meant that its development into an indigenous commercial capitalist class was rejected whether practicable or not.

### TANU Goals

The goals of TANU (Tanganyika African National Union - the sole party to win any parliamentary seats and subsequently the sole mainland party, merged with Zanzibar's Afro-Shirazi Party to form the CCM, Chama Cha Mapinduzi or Revolutionary Party, in 1977) relevant to commerce were:

- a. creation of an egalitarian society with a strong state economic role - there was a commitment to socialism but a very vague one not closely linked to immediate policy;
- b. increasing the African role in operation of the economy and the government;
- c. establishing - through the Party and government - effective African control over the economy;
- d. increasing the share of income and investible surplus received by Africans, African owned enterprises and the state.

These led to at least five concerns more specifically linked to the commercial sector:

1. fairness to African buyers who were (with some justification) believed to be discriminated against in terms of price by smaller enterprises and in terms of credit (and charges for it) by larger ones;

2. increasing the African (public or private) share of commercial profits (which were, on the whole, overestimated) at the expense of the absolute and relative share of foreign enterprises and non-citizens and the relative (not necessarily the absolute) share of privileged minority community citizens;
3. reduction of excess profits - somewhat vaguely defined - and profiteering - e.g. raising prices during and/or conniving to create brief shortages, raising tax paid stock prices after indirect tax changes;
4. use of state intervention as the central instrument for commercial sector change and linking it to a network of mass worker and peasant based consumer co-operatives;
5. less consistently encouraging individual African commercial units. In fact this was not energetically pursued even before the clear commitment to socialism in the 1967 Arusha Declaration. Compared to other African states, Tanzania spent little money on training or financing African businessmen; public sector banking and investment banking gave them little access to credit; licensing laws were never systematically used to discriminate in their favour.



C. First Steps - 1961/1966

The Tanzanian government moved rapidly to expand the public sector role both in the government subsector - e.g. through more comprehensive development planning and industrial legislation - and in public enterprise. It faced several constraints:

1. pre-independence Tanganyika had rarely balanced its recurrent budget, let alone had a surplus for investment;
2. the senior civil service were largely expatriate, with little public enterprise experience, facing major Tanzanianization (and training) as well as broadening and changing the scope of services provided and functions performed;
3. Tanzanian businessmen with experience even in middle sized businesses or middle level positions in large enterprises were dominantly from privileged minority community members, were in most cases not eager to become public sector employees and were in demand by European firms seeking to reduce expatriate salary bills and build up more respectable looking proportions of citizen managers.

These factors virtually required that state entry into the commercial sector be on a relatively modest scale (competing with not supplanting the large established firms); utilize European managerial skills for initial operations and for training citizens; and in some cases be on a joint venture basis. Certainly these characteristics of 1961-65 action could be justified on grounds of gaining experience without massive risks, pragmatic gradualism, perfecting the market by competition but, in practice, they were (as of 1961) virtually necessary choices if anything substantial was to be done rapidly with any real chance of success.

#### Intrata: An Initial Breakin

Three main lines were pursued - Intrata in general importing, Cosata as a co-operative apex commercial unit and strengthening of the Cotton and Coffee Marketing Boards.

Intrata was quite overtly launched to win a share of the general import business. It was a joint venture with a minor existing Netherlands firm whose ambitious manager saw a potential for a breakthrough as 40% partner and manager in a state trading unit he could never win from his existing private sector base. Intrata certainly won

a niche (perhaps 10%) in the major general importer top six but it never showed signs of becoming dominant or even challenging the leading firm. It was profitable; it did show more initiative in finding low cost sources of supply; it did hire - and to a degree train - Africans more rapidly than its competitors. Above all it proved that a state owned trading company need not be a disaster.

#### Cosata: A Debacle

That proof was important because Cosata quickly did become a disaster. It was intended as the import-export-wholesale centre for African retail cooperatives. The overall management was Israeli co-operative enterprise based. A quick takeoff was followed by a quicker collapse. Most - not all - retail cooperatives went bankrupt. Cosata - plagued by uncollectable receivables and unsaleable stocks nearly followed. Sharp complaints against the management's policies - asserted to damage Tanzania and discriminate against Africans - were followed by its firing. The development of retail co-operative (or indeed public sector retail more generally) was so discredited as not to become a live issue again until the 1970's and even then was pursued with a degree of caution and fearfulness clearly owing much to Cosata's debacle.

What went wrong? The management made two fatal errors. It assumed that because it knew what was sold by consumer co-ops in Israel it knew how to purchase for Tanzanian ones. Israeli oranges and wine were symbols of that error more than of a malign attempt to dump Israeli exports. Further it assumed that because any Israeli kibbutz could find a manager, a book-keeper, a committee able to run a retail co-op so could any Tanzanian rural or urban district; a misconception of truly stunning proportions in a country with (then) perhaps 15% adult literacy and with most of the (90%) rural population in isolated homesteads or hamlets. That private merchants sought to break co-ops by underselling selectively is doubtless true, given their advantages in stocking and management they hardly needed to bother.

The dream of co-operative trading as a quick route to African commercial sector participation was probably inherently ill founded. The success of crop marketing co-ops was misleading - their business management and accounting needs were less at primary society level and the strongest unions had been built by African "economic activists" before independence when their managerial positions were among the most attractive open to Africans. However, a more gradual approach linked to the stronger unions, including major training of society personnel and backed by a proper rural and urban shop sales survey might have

led to a successful, if modest, co-op structure. Certainly a limited number of African retail co-ops did remain viable - quite noticeably those with educated managers and committees including at least some businessmen or financial officials.

Cosata was not allowed to go bankrupt but refloated under Intrata management. By 1967 it had cleared its deficit and was - on the face of it - a profitable middle sized importer and large wholesaler specializing in textiles. However, this had been achieved by "confining" all textile imports to Cosata. While it did import and wholesale some, on the majority it charged a commission of about 2%-in theory for advice on what to purchase from whom but in practice usually for stamping documents already fully agreed by the actual importer and his source of supply. As a result, if anything, Cosata raised textile prices by confinement more than it reduced them by competition. Further it set a precedent for confinements as "private import taxes" which was to prove hard to control.

#### The Export Marketing Side

On the agricultural export side the primary society - union structures in coffee and cotton were well established by independence. These were strengthened and - much less uniformly successfully- new co-operatives were promoted

in other areas and crops. Three problems arose. Many primary societies - especially in lower education areas - were very badly and/or corruptly run. For low value crops and low density of sales areas, co-ops raised marketing costs compared to private traders who combined a variety of commercial lines while the co-op costs had to be covered by marketing alone. The societies - and more especially the Unions and the apex Co-operative Union of Tanzania - came to be dominated by richer farmers and by salaried managers.

Rural credit was placed in the co-op sector via three quasi banking institutions. A series of training programmes - including a Co-operative College for managers, accountants, committee members were created. While doubts arose, the basic criticisms that were to lead to the total disestablishment of traditional co-operatives by 1976 were still in the future.

The Cotton and Coffee Marketing Boards - which already existed and had some experienced expatriate management and selling experience - were strengthened. Here finance was not a problem - the Cotton Marketing Board ran large surpluses in a majority of years because its price stabilization was very cautious and the Coffee Marketing Board's first payment was cautious and its second made after proceeds and costs were known. The buildup of local auctions and -

especially in cotton - expert knowledge of world market behaviour leading to fairly adroit auction releases and minimum prices clearly gained foreign exchange for Tanzania, revenue for the Boards and higher prices (and/or more services such as cotton roads in the cotton case) for producers.

Over the same period considerable attention - involving the most able economic and legal personnel available to Tanzania (some specially imported for the purpose on a part time consultancy basis) was devoted to diamond marketing. For technical (number of grades, problems of preparing mixed packets), economic (a sellers' cartel is not easily surpassed by a minor independent sales organization) and mine ownership/management (50% De Beers/100% De Beers) reasons it was decided to continue to use the CSO. However, the CSO's commission was reduced, the royalty was raised and - perhaps most critical - an independent valuer chosen by Tanzania was interposed between Williamson's and the CSO as a check on valuation. By these methods Tanzania's revenues were raised absolutely and to 75-80% of total potential surplus. In addition rapid training was begun and closely supervised by Tanzanian Board members and (presently) senior managers with quite dramatic results within a decade.

Contexts and Goals Revisited

By February 1967 (the date of the Arusha Declaration which brought major changes to the state trading sector) there had been contextual changes:

1. Perhaps 12½-15% of consumer goods imports were by public sector trading companies and perhaps 5-10% of intermediate and capital goods imports by other public sector enterprises;
2. A limited foothold in wholesaling was held by state trading and manufacturing enterprises;
3. African produced crop marketing was increasingly co-op and Marketing Board run;
4. Retail co-operatives were perceived as non-viable; private African retail business had grown but was still a small proportion of total;
5. Public corporation development as publicly owned private enterprises with few distinctive characteristics other than ownership and moderately more speed in citizenization had proved competitive (but unlikely to become dominant rapidly) and financially viable (but hardly the highroad to Tanzanian control of the economy or egalitarianism).



The Party's goals had also evolved - largely for reasons quite outside the state trading sector's performance as such:

1. because a mixed economy led to foreign capitalism in Tanzania, a rapid transition to dominantly public sector ownership of the major means of production and trade was decided upon;
2. because the mixed economy route had proven inequalitarian, a much tighter control over wages and salaries was to be instituted;
3. because the combination of Party or public office and private business threatened to build a domestically dominant capitalist class dependent on foreign enterprise, a complete break between Party leadership and middle to higher level public sector employment and private business activity (including owning rental property and shares, serving as a director of a private company, having full time year round employees other than household staff) was to be enforced;
4. socialism, egalitarianism, self reliance and rural development were chosen - and both articulated and set into implementation as central organizing themes for Tanzanian development strategy.

D. Breakthrough and Crisis: 1967-71

By February 1967 the public sector capacity was greater than in 1961:

1. recurrent revenue was substantially above recurrent expenditure and local borrowing channels had been set up (further their significant enlargement was a part of the reasoning behind financial sector nationalization);
2. government departments and - to a lesser extent - public enterprises had substantial numbers of citizen staff, specialist expatriates with some analytical ability vis a vis public enterprise and the 1961-66 experience;
3. African managers were still in short supply - the manpower allocation system had in fact starved public enterprise of intermediate and "O level" personnel until the middle 1960's and only began to allocate significant numbers of university graduates in 1967-68 when Treasury and State House forcefully pointed out that, given a dominant state ownership position in large scale enterprise, common sense required a flow of managerial cadres to realize the potential for decision taking opened up by the ownership acquisition or creation.

4. Within existing cadres of citizen public enterprise managers (including those de facto hired by nationalizing the firms for which they worked) the problem existed that a disproportionate number were of privileged minority community ancestry - a situation exacerbated because the 1967-71 manpower allocation process allocated almost all new graduates from these communities to the public enterprises, not the civil service. The difficulty was not capacity nor - in any general sense - loyalty, but that to the "man in the street" or the "woman in the queue" the makeup of citizen managerial cadres quite literally "did not look right". The only source of experienced citizen managers of African ancestry was the civil service.
5. Because the 1967 nationalizations were broad front designed to create a dominant state position in manufacturing, milling and finance as well as external trade, the opportunity cost of personnel and time was high. Realistically only one sector could be managed directly - i.e. without a managing agent - and for both broad political economic and quite specific contextual reasons that sector was finance.

### The Acquisition Exercise

In the case of trade the acquisitions comprised 14 odd (some very odd to the point of purely paper existence) firms, or their Tanzania assets and liabilities, plus the minority private interest in Intrata. Excluding Intrata there were four substantial enterprises (or six if one treats the three Smith McKenzie group subsidiaries as separate companies) whose main operations included:

1. about 20-25% of total imports or over 50% of final consumer goods and perhaps 10-15% of intermediate and capital goods imports;
2. a modest overall export turnover specialized in minor products e.g. beeswax, wattle extract;
3. a central position in the initial distribution/wholesaling of imports to main towns;
4. the majority of the shipping agency business.

The initial overall management of the new State Trading Corporation (which was a holding and management company with the acquired firms, Intrata and Cosata as operating subsidiaries) was entrusted on a management contract to the ex-minority partner in Intrata. Most of the expatriate senior staff of the acquired enterprises were kept on secondment (or analogous arrangements) from the parent

companies terminable at the discretion of either side. Citizen and permanently resident non-citizen employees (the middle management were largely British citizens of Asian ancestry born and permanently resident in Tanzania) were given employment in the STC group on the same terms and conditions they had enjoyed in the acquired companies as part of the nationalisation legislation.

The short term restructuring related largely to turning the subsidiaries into specialized functional units (e.g. textiles, exports, shipping agencies, food, general merchandise) with related transfers of personnel and use of assets. Internal staff training was begun - perhaps not very systematically - and a significant number of citizen managerial candidates secured from the civil service and new graduate allocation. (STC developed tendencies toward overmanning at managerial levels and did expand, so over this period no significant reduction in overall expatriate or resident non-citizen numbers was achieved - indeed, quite the reverse - though the proportion relative to citizens fell sharply.)

The initial formation process of STC was constrained on the one hand by the goals of securing a dominant position in the general import trade and of operating without a transitional crisis or an enterprise deficit and by the constraints of limited public sector personnel for operation or supervision

and of heavy competing demands for them from other newly acquired enterprises. This is the context in which use of a known expatriate firm and its known managers as a central management contractor and of securing - at least for the initial period - the continued services of existing acquired enterprise expatriate and non-citizen personnel was seen as the only prudent course of action.

The Management Agreement lasted for about three years during which STC was consolidated. At that point STC was shifted to Tanzanian management but with extensive use of McKinsey as consultants on a variety of issues including recruitment and operation as well as broader structural and strategic reorganization and planning.

#### Notes on Nationalisation

Three special characteristics of nationalisation require mention albeit they cannot be pursued in detail:

1. in these cases the initial handover and phasing out of ex-owner staff was smooth and the negotiation of compensation, while time and talent intensive, neither very embrangled nor resulting in sectoral payments in excess of (or even as high as) sectoral public enterprise post tax profits;

2. a remarkable number of discontinuities (such as assets having no real relation to trade acquired e.g. cement company shares, sisal estate mortgages); Tanzania companies owning or investing in other country based units of the same group; trading assets not owned by the trading company (e.g. the warehouses of one group owned by an unacquired building holding unit not the acquired trading units) were discovered and required tidying up;
  
3. the impact on private investment in trade was not homogenous although until 1971 it was fairly modest. General import/export private investment was nil - but that was state policy; specialist import firms were not, on balance, much deterred from expansion. Wholesaling and large retailing if anything grew more rapidly over 1967-71 than previously; small and medium African private retailing continued its limited and uneven growth. A crisis situation in a number of wholesale and retail sub sectors (and a milder retrenchment in specialist importing) did occur in 1971 as a result of nationalization of large rental properties and was followed over 1971-73 by an attempt to raise retail margins drastically to maximize returns before further public sector expansion (or to recoup losses on buildings).

The first of these elements is moderately typical of nationalization (at least when compensation of some variety is credibly proposed). While in one sector (not trade) a 90 day withdrawal of ex-owner senior staff forced earlier reorganisation than planned, only one case (again not in trade) even approximated the nightmare of taking over a closed enterprise with senior staff gone, no coherent handover and the firm not in working order. The second element is typical of almost any acquisition of existing firms - enterprises, like people, acquire rather odd collections of things and arrangements over their lifetimes. The third is not predictable except in the sense that nationalisation or rapid expansion of public enterprise in general is unlikely to have positive effects on overall private investment. In Tanzania, despite a fairly clear policy of transition to socialism, investors were apparently seriously deterred only if their own enterprises or ones very similar to them had been directly affected.

During 1967-71 buildup of public sector export marketing was consolidated, with co-operative coverage becoming almost total for main export crops collection and marketing boards performing a similar role for sales to exporters. The main hides and skins exporter was acquired as a joint venture - a byproduct of the import trade nationalizations. Promotion of retail co-operatives as part of the development of communal villages was pursued in a low key - and some



success, perhaps up to 10% of rural retail trade - from 1969 on while occasional higher profile calls for mass launching of co-op shops were limited in duration and had negligible (positive or negative) impact.

STC under McKinsey advice launched a major centralization exercise: merging subsidiaries into the parent company, seeking to operate ordering and inventory supervision totally centrally, proposing a unified computer programmed accounts system, etc. In the process it massively expanded central office staff acquiring a significant number of new expatriates - virtually uniformly more modern and less experienced, more expensive and less interested in Tanzania than the (smaller number) "hold over" expatriates they replaced. A more unambiguously positive component was a citizen training programme at all levels.

#### Structural Shifts in State Trading

Since 1966 the share - indeed the absolute physical quantity - of consumer goods imports was reduced both by increased domestic production and by tighter import controls. The share, physical volume and value of intermediate and capital goods imports rose. This had complex results on the role of individual public sector firms:

1. STC was specialized in a relatively declining sector of the import business and found that, despite building up its share of those goods it did handle, its share of total imports was stagnant;
2. further it continued to show a bias toward importing versus wholesaling local products (largely because certainty of delivery and quality, ability to place large orders with single firms, availability of 180 days' credit and use of standard business procedures made the import business seem simpler) so that its share of wholesaling probably shrank;
3. the manufacturing sector public enterprise imported their raw materials and intermediate goods direct and handled their own wholesaling. In addition in a few cases they also handled imports of competitive products (e.g. shoe imports were for a time confined to the domestic shoe company which, admittedly, had been the largest shoe importer before nationalisation, but by no means the only one);
4. the gradual acquisition/establishment of more public enterprises (including two joint venture cases accounting for about 60% of the petroleum importing and distribution) meant that overall the public share in import and wholesale trade was growing significantly while STC's share in state trading was falling and no real coordination existed for the balance of the sector.

STC's response was to seek:

1. to have imports of more goods "confined" to it - including specialized parastatal imports on which in fact it charged a fee for stamping papers prepared by the users;
2. to launch takeover bids for a variety of specialized importers.

Although sweeping plans were articulated, the second wing of the expansion campaign was only carried out to a small extent. The first went further and, unfortunately, raised costs to users while muddling some orders and delaying others. Asserted gains in finding lower cost sources were in part real, but probably at the best offset the fees charged on those products.

STC also initiated three further changes:

1. buying for cash on shipment instead of 90 to 180 days credit (apparently because the treatment of costs was such that this appeared to purchasing officials to raise profits because they did not offset the interest on domestic overdraft);
2. introducing pan-territorial prices (i.e. uniform for from 6 to 30 towns instead of based on Dar es Salaam plus transport) for a significant number of goods (unfortunately in most cases by taking the Dar es Salaam price as the uniform price not working out "transport equilization" fund principles (as had been done in

sugar and petroleum products when similar pricing had - much earlier - been applied to them);

3. rationalizing and restructuring markups - partly to make those on luxury goods higher than those on necessities, but largely to offset the extra costs from a larger headquarters, the greater interest bill and the loss on pan-territorial pricing as it was actually handled.

### STC in Crisis

Over 1970-71 STC plunged into a complex crisis which ramified far beyond state trading:

1. the centralized control system failed to function so that knowledge on stocks and sales was notable for its absence or inaccuracy;
2. as a result inventories by item ranged from 14 years to minus 3 months (presumptively an accounting system error) with a rapid buildup of total stocks to total turnover paralleling an even more rapid rise in out of stock items;
3. the endemic shortages were exacerbated up country by delays in getting data and arranging transport so that rural areas were starved of basic imported consumer goods;

4. the group slid into the red for fiscal 1969/70 and its 1970/71 recovery (not known at the time given the state of accounts) was probably spurious given unsaleable stock buildup;
5. the shift to domestic bank (from foreign supplier) credit caused a once for all decline in foreign exchange reserves in 1970 and 1971 of perhaps \$20-25 million as well as an alarming explosion in domestic credit formation - a pair of developments unfortunately coinciding with other strains on the foreign position to create a reserve crisis in 1971-72.

These developments created widespread alarm and massive reaction:

- a. the Bank of Tanzania and the Treasury intervened to set interim domestic credit ceilings and import licensing controls and took steps to develop comprehensive domestic credit and foreign exchange planning;
- b. Parliament set up a committee to examine shortages and breakdowns of distribution;
- c. the Ministry of Commerce and Industry set up an Inter-ministerial Working Group (Internal Consultancy Team) to analyze what was wrong and to report back.

The underlying concerns were both political and technocratic. First, it was perceived that the speediest way to discredit transition to socialism was to allow it to be seen that it - literally - could not deliver the goods. Second, starving rural areas of basic goods was hardly consistent with a rural development national strategic emphasis or with encouraging increased marketed output. Third, to allow domestic credit and foreign reserves to flow away like blood from a cut artery would quickly destroy the capacity to meet bills for vital imports and/or deliver Tanzanian strategy into the hands of its creditors. Fourth, with the bulk of large scale enterprise in the public sector, unplanned deficits would destroy both the company tax and investible surplus bases for public service and productive investment expansion.

#### Goals and Constraints - End 1971

The state trading constraints of the end of 1971 were largely conditioned by the STC crisis:

1. rapid reduction of shortages and building a distribution system capable of preventing their recurrence;
2. ending the uncontrolled loss of foreign exchange and equally uncontrolled rise of domestic bank credit;
3. reversing the slide into deficit (the 1970/71 apparent turnaround not being known) and doing so without causing additional inflationary pressures.

These were constraints - not goals - in the sense that they were seen as vital to limit the damage to public confidence, development momentum and internal/external financial stability. Equally they outweighed any general contextual factors so far as the state trading sector was concerned.

The goals directly relevant were:

1. to rationalize the overall state trading sector (not just STC);
2. to develop a system of price management which would protect consumers from margin inflation/inefficiency and also protect enterprise surpluses (and company tax) so long as they were moderately well run;
3. to build up coherent domestic credit and foreign exchange budgeting;
4. to relate the 1971 Party Guidelines emphasis on decentralisation and participation to the state trading sector.

E. Recovery and Development, 1972-78

January 1972 again showed a significant increase in public sector capacity - albeit in relation to state trading this was at the time open to serious question:

1. the domestic recurrent revenue and credit position was markedly higher (if under greater strain because of even more radically expanded capacity to utilize resources) and the technical competence of and Tanzanian control over the public financial sector (state and financial enterprise) vastly greater than five years before;
2. the fact that an Interministerial Working Group which was in fact a consultancy team could be created with a majority of citizen members (and the three expatriates Tanzania ministry staff, not outside consultants) bears witness to the increase in public sector experience and competence vis a vis public enterprises, and the fact that this was done in respect of a firm which had gone into crisis while receiving detailed consultancy from McKinsey and company shows a parallel shift in confidence in domestic capacity;
3. the number of African managers had risen sharply. With the influx of graduates and additional training of former clerks, foremen and middle managers, so had their qualifications while with the passage of time an increasing number had substantial experience behind them;
4. because most of the rest of the public enterprise sector was operating in the range passably to very well and the other problem cases did not have major macro spread effects, attention could be concentrated on STC in particular and state trading more generally;



5. similarly the number of successes elsewhere in the public enterprise sector led to a belief that STC was a problem to be tackled with good chances of success not a symptom of any general and inherent pathology of public enterprise. This view was especially strongly held by the public institutions (e.g. Party, Treasury, Bank of Tanzania, National Bank of Commerce) most urgent in their calls for root and branch reform. Their demands for radical change were grounded in a firm belief substantial improvement on a sustained basis was attainable.

#### 1972 - Patching Up and Planning Ahead

Within STC a patching up exercise had been begun in 1971. As a holding operation this had marked success. Credit control forced halting purchases of overstocked goods and public pressure rebuilding supplies of these endemically unavailable. The process of debating credit with the NBC itself forced better identification of stocks and flows, facilitated by a reversion to rather rough and ready data collection which (unlike their sophisticated, centralized immediate predecessors) usually produced approximately correct figures in time to be of use. Further the pressure to get goods into stock and out to retailers forced de facto deconcentration of decisions which had previously piled up untaken on two or three desks. Shortages at least ceased

to escalate and to some extent declined, credit use stabilized as did demands on foreign exchange, cash flow and surplus recovered fully (at least on paper - writeoffs of dead stock over 1972/73 - 1974/75 make comparison of year to year results over 1969/70 - 1973/74 of dubious utility). Indeed by mid-1972 STC was showing signs of being able to cope at least in the absence of a new exogenous shock (e.g. a foreign exchange crisis). However, this was not a symptom of development or true structural reform but of partial reversion to the 1967-69 style of operation.

The patching up was essential in allowing the Working Group time to concentrate on analysis and preparing proposals for more basic (and necessarily longer term) structural change. In its absence either STC would have collapsed or - more realistically - the Working Group would have become an emergency management team.

The analysis - somewhat hampered by STC's lack of data on what had been happening and the inability or unwillingness of most (not all) of its senior managers to appear to discuss problems with the group - is in effect summarized in the previous historical sketch. The key weaknesses identified were:

1. overcentralization of everything leading to;
2. decisions piling up untaken on a handful of desks;
3. a data collection and analysis "system" quite unworkable given Tanzanian data recording and transmitting capacity and quite unnecessary to handle the relatively simple (in large trading enterprise terms) STC business leading to;
4. near complete lack of knowledge of sales, stocks, purchases, debts on any up to date basis and therefore;
5. an inability to get the right goods to the right place at the right time.

The Working Group was not unanimous on how to proceed - its advice in mid 1972 to the Minister presented options of which the one embodying the greatest decentralization and the most radical structural changes was chosen. Its articulation and implementation - which was basically completed early in 1974 with at least half was introduced by mid 1973 - was placed in the hands of a second Working Group, this time of selected managers who were subsequently to serve with the overall coordination/control body (Board of Internal Trade) or new state trading units.

The new structure included:

1. Regional Trading Companies to handle general wholesaling in each region (imports and an increased share of local manufactures) serviced as to imports and some intraregional

trade in manufactures by;

2. a series of specialized National Trading Companies (e.g. Agricultural and Industrial Supplies, Food, Textiles, Household Supplies);
3. which in the case of technically complex products (e.g. Pharmaceuticals) and those requiring after sales service (e.g. some machinery and equipment) also carried on wholesaling;
4. two non-STC successor wholesale trading companies - Texco for domestically produced textiles and National Milling for grains and certain other staple foodstuffs (which it also was responsible for purchasing domestically and importing) and a number of wholesale (and to a lesser degree import) divisions of manufacturing parastatals e.g. Wood Industries Corporation, Steel Rolling Mill);
5. a Board of Internal Trade (rather oddly titled given the high import share) responsible for overall coordination, supervision, data analysis and personnel development of the public trading sector (with the exception of NMC and exports and with special responsibility for the STC successors) and with the duty and power (used at least once) to take over interim management of any company descending toward a crisis.

Each company was (is) self managing. The radical reduction in range of products and number of units was intended to simplify data collection, purchasing, distribution, inventory control and financial management. It appears to have had that result - at any rate the subsequent record has been of more timely, better informed decisions and a reduction in numbers both of "overhead" staff and of expatriates.

The STC successor companies are formally owned by the Treasury - to make financial supervision and control easier. The Regional Trading Company Boards are largely regionally appointed, all Boards include worker and Party representatives.

#### Agriculture and Exports

Over the same period the export and food crop sub-sectors of state trading were also restructured. The Union and Cooperative Union levels of the Co-op sector came to be perceived as dominated by rural elites antagonistic to egalitarian socialism, economically inefficient at the expense of peasants and/or urban consumers and quite outside effective Party or government policy or planning control. In 1971 the CUT's rural credit institutions were taken away from it and made into financial sector parastatals. In 1976 the CUT and Unions were abolished and their functions

as traders turned over to the Crop Authorities (NMC and the successors to Marketing Boards). The primary societies were abolished as such but their functions were turned over to the Village Councils of the 7,000 odd villages resulting from the 1967-76 (and especially 1974-76) alteration of rural settlement patterns from 85% dispersed to 90-95% in substantial villages.

The Crop Authorities (some of which have production support responsibilities) handle domestic purchasing, processing, domestic wholesaling (e.g. cotton to textile mills, cotton seed to oil mills), export sales (at domestic auction, by direct negotiation in Tanzania, to a degree direct to European markets). NMC handles about ten food (and minor export) crops with parallel responsibility for imports (or exports) to balance local sales and purchases where necessary for grains. The Sugar Authority has a parallel import/export and supply/demand balancing role for that crop.

#### Urban and Rural Retailing

State trading in the retail field has been at two levels - District Development Corporations and village (or to a much lesser extent urban neighborhood) shops. The first - in meat, petrol and less often other products - had a

nearby uninterrupted record of failure. On the whole goods were supplied (and exceptions, e.g. Dar meat, often related to conditions beyond the trading units control) albeit at a lower standard of service and quality than the private predecessors. However, cost control was notable for its absence and losses for their ubiquity. Workable managerial and staff development systems were nearly unknown - perhaps a criticism of the BIT as much as of the decentralized units, but a criticism to which the answer that all it could do was to supervise essential reconstruction and running in of the import/wholesale state trading structure would be almost wholly valid. Thus as of 1978 urban public sector retail trade was limited to a handful of consumer co-ops and a small but growing number of retail outlets run by wholesale firms.

Village shops had a mixed record - enthusiasm often outran capacity. However, with the use of personnel trained at the Co-op College or in the very large and diversified 1974-78 Adult Education programme, a growing number of Village Councils (perhaps approaching a half) had established viable retail shops by the end of 1978. The access to an articulated, functioning state trading sector at wholesale level, the relatively limited number of lines demanded (simplifying purchasing - stocktaking - accounting) and the retreat (partly for political but largely for

economic reasons) of many of the non-citizen retailers to urban areas or abroad have created a climate more "technically" propitious than that of the early 1960's while 10 years of transition to socialism, broad adult literacy, and effective (in most cases) village councils have created a more supportive political setting.

### Parallel Actions

A series of major policy and institutional changes over 1972-74 significantly altered the context within which the import and wholesale side of state trading operated. These were part of the general buildup of planned control of resource allocation as part of implementing the transition to socialism and also part of a fairly clear pattern of Tanzanian response to crises by seeking to cope immediately while creating a set of institutions and decision taking supports to avoid domestically generated and limit externally generated recurrences of the same crisis.

The most important were foreign exchange and credit budgeting, import licensing and "transfer price" checking, overall domestic price management and tightening of supervision over public enterprise annual physical/financial planning and use of surpluses. These can only be sketched here



but are critical to the understanding of the altered environment in which state trading in Tanzania operated by the mid-1970's: one of quasi imperative planning with a state near monopoly over external trade and finance but with very considerable reliance on managed (rigged) markets and no pretence whatsoever of material balances planning beyond a handful of key commodities such as grains.

1. Foreign exchange budgeting by import category gave indicative purchase limits to state trading importers - limits subject to some adjustment in respect to price changes for key individual imports and to a broad degree allocable by the firm within fairly broad import classification categories;
2. Domestic credit budgeting set overdraft ceilings and therefore guidelines on possible total of inventories and receivables;
3. Taken with foreign exchange budgeting it created incentives to use 90-180 day credit from sellers, develop domestic sources of supply, reduce receivables outstanding, monitor ratios of inventory to turnover on a line by line basis and achieve a cash flow surplus to allow larger turnover and financial resource availability.
4. The budgets were worked out in some detail by the Bank of Tanzania and Treasury/Planning with support on articulation from the NBC and some consultation with major credit and foreign exchange users.

Implementation was in NBC hands on credit and a new Import Licensing division (seen as the logical extension of exchange control) in the Bank of Tanzania;

5. Monitoring of physical correctness of shipments and discrepancies of prices from general norms was contracted out by the Bank of Tanzania to General Superintendence (a Swiss specialist firm) - without its clearance stamp no goods could be imported nor remittance made. Similar monitoring of major service contracts was carried out internally by the Bank of Tanzania and Treasury/Planning;
6. The somewhat narrowly titled Limitation of Dividends and Surpluses Act of 1973 and its 1974 Amendment created a set of powers (yet to be implemented for all public enterprises) for the Commissioner of Public Investments to require annual trading and capital plans/budgets in physical and financial terms from each public enterprise. The BIT group of companies were among those in respect of which this procedure was first implemented;
7. Following the 1973 devaluation a Task Force studied the mechanics of creating a price management body. Its report informed the 1973 Prices Act and its initial set of importer/manufacturer - wholesaler - retailer posted prices. The approach was one of price

and margin management not price control in the traditional sense. In the process of creating the new body, the Task Force and the emerging BIT group carried out a rationalization of state trading margins (probably on balance reducing them) and a distinct narrowing of some retail margins. This was workable in 1973 because the rising efficiency of state trading and a relatively relaxed import control (the balance of payments was for exogenous reasons strong from early 1972 to the last quarter of 1973) meant that goods were more readily available (allowing squeezing of recently inflated margins) and that state trading margin freezes or cuts did not threaten the companies with bankruptcy.

Facing Exogenous Crisis: 1974-77

The combination of back to back droughts in 1973 and 1974 and the impact of oil and related manufactured goods prices inflation made Tanzania rank number 3 on the UN's "most severely affected" list. An UNCTAD estimate showed that the 1972-74 loss of national purchasing power from terms of trade shifts alone was of the order of 11-12%. The resultant strains on state trading and the related institutions sketched above were severe.

Not surprisingly a series of problems arose in respect to the state trading sector:

1. the NMC while consistently good in projecting grain availability and demand initially failed to operate adequate external procurement leading to a short 1974 physical shortage of supply - a breakdown fairly speedily reversed and not repeated;
2. somewhat slow adjustment of retail grain and sugar prices to meet the skyrocketing prices (and increased share) of imports led to large 1973 and 1974 deficits. Mid and late 1974 price increases (as part of an overall price - wage - tax adjustment package) returned the NMC and Sugar Corporation to profit and the deficits were wiped out over 1975-77 as domestic supplies (cheaper than imports even after substantial grower price increases) replaced imports so that grain and sugar prices were not increased after November 1974 (indeed sugar and rice were reduced in 1975/6);
3. with draconic import controls (relative to the size of the economy the physical volume of imports in 1976 was 40% below 1973 and for consumer goods other than staple foods and inputs into consumer goods manufacturing the compression was over 50%) even improved inventory control and distribution could not avert increased shortages. These were particularly acute in rural areas. However, in contrast to the earlier crisis

the core of essential goods (e.g. bread, grain, oil, sugar, salt, cloth, matches) were less frequently and more briefly out of stock - the long gaps were in semi-necessities and amenities;

4. a resurgence of private manufacturing of semi-necessities and amenities occurred over 1975-77 with very few marketed via state trading bodies. This certainly reduced shortages and pressures on the BIT group but also eroded the public sector share of wholesale turnover;
5. as of mid 1974 almost all imports were confined to a limited range of state trading units - basically the BIT group, NMC. This did simplify import licensing as a means to implement the foreign exchange budget but - as before - raised costs, delays and inept procurement for firms using products in respect of which the BIT group had no expertise;
6. price management - even though based on forecast as well as past costs - had a tendency to squeeze actual margins (at least in % terms) by underestimating costs and to squeeze cash flow because of attempts to hold increases to one or two a year (with high margins early in the period to average out with low ones later).

These problems are hardly surprising given the degree and duration of the crisis. What is surprising is how well on balance the state trading enterprises and related institutions

coped. Basic commodities were procured locally, imported, distributed without endemic shortages or major profiteering. After a traumatic adjustment to new world prices (about 50% on the retail price index in late 1974 and early 1975) inflation was held at 10-15%, below the world average or the import price average for much of the period. The state trading sector on balance continued to achieve substantial surpluses while making the Price Commission's control side workable.

Over 1977-78 confinement was phased out in respect of public sector and large private sector users of specialized machinery, spares and raw materials/intermediate goods. This change was seen as a permanent one, not merely part of the general (indeed too general) relaxation of import controls of late 1977 and early 1978. As of late 1978 a renewed foreign exchange crisis had arisen but - at least on the import side - had little relationship to state trading.

Agricultural export volume in 1978 was lower than in 1966. However, it is not clear that state trading was itself more than peripherally implicated in this failure - collection and payment had, if anything, improved over the period. Centrally marketed basic foodstuffs had doubled in volume - NMC clearly did improve collection

and payment and 1974-78 price policy was more favourable to domestic food than to domestic industrial input or export crops. In respect to non-agricultural exports relatively little (beyond the existing diamonds case) had been achieved - initial experiments with textiles had ended with domestic demand exceeding supply and sisal twine and cashew kernal exporting was still in its initial trial and error stages.

#### 1979: Context and Goals

Tanzania in 1979 is structurally very different from 1961 but remains very poor and very subject to exogenous shocks from the weather and/or international economy changes. In respect to trade:

1. It is now carried on in what is more a planned (rigged market) than a "free" market economy;
2. The bulk of imports, exports and wholesaling are in the hands of a relatively decentralized state trading sector;
3. A series of institutions and procedures - Prices Commission, annual enterprise plan review, Credit Budgeting, Foreign Exchange Budgeting, BIT - exist to provide operational guidelines for and direction over the state trading enterprises;

4. nothing works quite as well or as consistently as intended - secondary mistakes are frequent and sometimes serious;
5. but over 1974-77 the system did surmount a crisis avoiding starvation, mass discontent, halting expansion of public services, radically cutting investment and returning to significant (4-6% real) output growth after a one year gap;
6. managerial and institutional experience is growing and is now predominantly Tanzanian not expatriate;
7. retail trade in the urban areas is still dominantly private (say 90-95%) and non-African (say 80%). It is now, however, in a planned economy setting and subject to a not insignificant degree of control;
8. rural retail trade is swinging toward decentralized state trading although at present up to three quarters remains private and up to half non-African;
9. while there has been a revival of confidence in rural decentralized state trading the doubts as to its urban viability have been reinforced. In the more complex and competitive urban retail setting, the opportunity cost (especially in terms of training and of personnel) of building up dominant local government related or co-op retail stores is implicitly assumed



to be prohibitive - implicitly because the question has never been fully reviewed since the Cosata debacle and hardly raised at all since the 1974-77 failures in District Development Corporation trading.

Party goals as of 1978-79 do not appear to have elements requiring radical short term alteration, as opposed to consolidation and efficiency improvement, of state trading:

1. greater emphasis on production (especially domestic foods and exports) to reduce vulnerability to external shocks and increase self reliance may lead to review of the export marketing sub-sector of state trading;
2. the liberation of Uganda is more likely to place strains on public sector transport than on state trading as Uganda/Tanzania trade was never large and is not likely to become so without medium term planned production coordination;
3. However, the liberation of Uganda, like the concerted struggle for the liberation of Southern Africa, does lead to possibilities and requirements for trade expansion with regional countries. State trading has been weak in that arena (even while the East African Community existed) and a rethinking of how existing units can acquire data and capacity to place exports/secure imports or a new specialized trading unit may be needed.

4. at some point - probably before 1985 - renewed emphasis on taking worker participation further (requiring rethinking, reeducating and restructuring in existing state trading units) and on pushing the phase down of capitalism much further in urban retail trade (requiring serious attention to this sub-sector) is almost certain. However, it is unlikely to be in 1979 or 1980.

### III

#### F. Issues and Articulations

State trading is not an end in itself. Therefore the goals or targets for a state trading enterprise or sector should be identified before considering particular coverage, methods of initial entry and constraints.

At least there clusters of goals can be identified from the Tanzanian experience: gross national product and surplus enhancement, consumer protection, broader political economic transformation. State trading can, in principle and in some contexts, be relevant to each - it is rarely likely to prove an adequate complete approach to any.

Surplus/GDP

- a. lowering the cost of imports (price of exports) by buying from (selling to) different enterprises or on different terms and by eliminating transfer pricing abuses resulting from importer/exporter transactions with jointly controlled companies. To achieve this requires personnel with knowledge of the relevant product markets and access to up to date data - bad buying (selling) can be more expensive than collusive trading;
- b. augmenting national (especially public sector) surplus by acquiring the surplus flow previously going to private traders and/or by raising trading margins. To achieve the former requires competent management (albeit if the only aim is to hold existing surplus levels it entails less external purchasing expertise). The latter - margin raising - route is simple) but in general would appear to be inferior to general or selective tax increases yielding the same revenue;
- c. providing a set of institutions more co-operative with the exchange control authorities i.e. not likely to engage as principals or agents in capital flight. This requires that the state trading enterprises are dominant in import/export and especially in general goods with many alternative external sources and domestic traders;

Consumer Protection

- d. price control implementation via margin limitation (for the state trader) and control (for private traders buying from it i.e. enforced retail price with halting of supply as penalty for breach). This requires a dominant import/wholesale position in the goods to be controlled and a flow of goods not radically below "controlled" retail price demand so far as controlling retailers goes. On margin limitation it requires excess initial margins, greater operating efficiency or acceptance of a lower surplus (or a loss);
- e. improved availability of goods through altering the mix of procurement (e.g. more priority to staples) and/or the priorities in distribution (e.g. basic up-country shipments first priority) may be more critical to consumers (including small traders and manufacturers) than marginal price changes. To achieve this goal requires data on demand by product and province plus a well functioning stock reporting system at least down to provincial level and a relatively smoothly working transport system to up-country depots;
- f. reducing selling (buying) price differentials by setting uniform (or less unequal) prices nationally or for a number of specified points benefits up-country buyers (producers) either at the expense of those

nearer main towns and ports (if transport equalization costs are computed and new prices set to retain surplus) or of public sector surplus (if - say - uniform prices are set at the old metropolitan price level). The setting of such prices on a wide range of products with substantial transport costs is very time consuming if mistakes leading to surplus loss or unintended "reshipments" are to be avoided;

#### Political Economic Transformation

- g. citizenisation of senior personnel combined with national ownership can increase self reliance and national control over economic decision taking. This result requires training of citizens and overall public institution attention to trading to ensure that state trading citizen management is or becomes present, effective and acting in ways different from its predecessors;
- h. decentralisation can be promoted or strengthened by placing state trading units in the hands of provinces or local councils. For this to have a positive effect it is essential that the decentralized units be able to operate/control the enterprises;

- i. transition to social democracy with a substantial state direct economic role, to state capitalism or to socialism requires a significant state trading sector. The exact requirements on the enterprises depend on the nature and speed of transition envisaged.

These goals are not necessarily alternatives any more than they are necessarily present in every state trading sector or enterprise. Unless the state trading sector is perceived as a desired channel of (rather random) consumption transfer payments, some surplus generation considerations will be almost universally present. Beyond that it is difficult to generalize about particular enterprise or even sectoral goal makeup and prioritization.

### Sectoral Coverage

Appropriate sectoral coverage depends on goals and capacities. This sounds trite but is often overlooked - import houses do not eliminate retail overcharging nor domestic produce collection systems solve problems of abnormally and artificially low export prices.

The main sub-sectors are importing, wholesaling of imports and domestically produced goods, export produce collection, exporting and retailing. The last is not particularly suitable for centralized state trading and the buildup of co-operative or local government enterprises to handle it tends to be arduous and slow.

Within each sub-sector, different products have different characteristics. A wheat flour importing - local purchasing and milling - distribution and wholesaling operation is quite different from automobile and lorry importation - stocking - sales - service. Similarly copper metal and concentrate exporting pose different problems. It is quite untrue that experience in one sub-sector or product is necessarily relevant to others - especially at purchasing and selling levels.

There is no a priori case for one unit in each sub-sector. Importing and wholesaling may usefully be combined if a limited number of products with similar distribution patterns and a total turnover of under \$20 million are involved. Equally if total imports handled exceed - say - \$50 million a case for specialized, multiple import enterprises is likely to exist.

### Initial Entry

Except in the context of a literally revolutionary governmental and political economic transformation, initial entry is likely to be partial even if it is intended to create a dominant state trading position in the medium term. Experience, institutions and personnel built up before massive expansion can increase capacity for further development. On the other hand, purely nominal entry -

especially as a minority partner in a joint venture - is unlikely to give much relevant experience or alter the structure of commerce significantly.

The choices in respect of initial entry include:

- a. nationalization (or majority joint venture with) existing private firm, joint venture with new private partner, building a trading wing onto an existing public enterprise, creating a new public enterprise;
- b. using old (expatriate) management under a management contract, negotiating a management contract with a new foreign firm, self management (including direct hire of any expatriate personnel needed);
- c. setting out to achieve a commercial success on fairly standard business lines first, initiating structural changes first or seeking to balance the two sets of aims from the start;
- d. initiating state trading largely or exclusively in one sub-sector (or one geographic area), in several selected areas, or on a broad front.

Little can be said about the appropriate choice in the abstract. In general the first choice listed is the least risky and least likely to produce radical changes and the last the most difficult to operate successfully but also the most productive when it is possible to implement efficiently.



The greater the scope of the initial state trading field (and therefore the greater its capacity to create crisis if it goes wrong), the less the experience and personnel available to the state and the greater the need to achieve initial successes to bolster public service and public confidence, the stronger the case for initial choice of a low or intermediate risk option. First steps need not be last steps if they are in the right direction and help in discerning the further course of the trail.

#### Expansion Targets and Trajectories

How fast and far state trading should be expanded depends partly on resources available, partly on performance but most on the purposes it is intended to serve. If these are limited to increasing competition and earning a return on state investment, normal commercial criteria apply. If they relate to providing basic goods, wholesale depots and produce buying points up-country a planned buildup of coverage to all provinces over five years may be appropriate. If effective state control over foreign exchange and surplus is sought - whether as an integral part of a transition to socialism or otherwise - then priority must be given to building up the state trading position to dominate import and export trade (and probably wholesaling) and to be strong enough to enforce some

limits on private wholesale/retail margins and price patterns. In the last case a decade is a not unreasonably leisurely time span, but it should be used to set and achieve interim targets, not justify delay.

Crisis affect buildup in various ways. If generated within the existing state trading system they usually require a delay for revival, reconstruction and consolidation. If external, they may - e.g. predatory competition by or sudden departure of major private firms - require emergency expansion or may - e.g. general foreign exchange crisis and import controls - create a case for a broader state trading role (to help implement controls and to cut the scope for "entrepreneurs of adversity" using shortages as a highroad to riches) at the same time as making it harder to achieve, because financial and personnel resources are under more than normally severe pressure.

### Constraints

State trading development will be constrained to the extent any or all of the following are in scarce supply:

1. public sector finance (including borrowing capacity) for premises, vehicles, stocks and receivables;

2. public sector institutional experience and capacity in respect to public enterprise in general and state trading in particular;
3. public sector knowledge (and ability to acquire more rapidly) in respect of the existing commercial sector (including domestic and external sources, markets, prices) and of relevant state trading experience elsewhere;
4. public sector ownership or ability to acquire suitable functioning trading units and/or their assets and contacts;
5. citizen personnel with relevant training and experience to staff state trading enterprises and related public sector units (e.g. Board of Trade, Price Commission, Import Control, Co-operative Development);
6. public sector capacity to secure expatriates with training, experience and loyalties relevant to filling gaps in citizen cadres - including training citizen replacements;
7. public sector self confidence and public confidence in the public sector as able to reach targets, achieve desired changes and - in particular - operate business enterprises.

Constraints do not normally prevent action - they limit how much can be done how soon and how well (and by whom in respect to use of expatriates to augment citizen personnel). One major goal of first steps is to produce resources which loosen the constraints and allow further development.

The most general constraint, however, is what else needs to be done i.e. the opportunity cost of creating or expanding state trading in terms of something else left undone or postponed. Negotiators on copper mine taxation or development cannot at the same time negotiate on establishing an import/wholesale corporation or an agreement with a London brokerage house on a joint marketing operation for coconut products. Accountants of wholesale depots are not available to staff provincial tax offices. Bank credit used to finance inventories of state trading ventures cannot be put into Treasury stock to finance a hydroelectric station.

How much of each scarce resource can reasonably be devoted to state trading at any time depends on what importance and temporal priority is given to it. Firm allocations limited to resources likely to be available in the first place offer a better planning and implementation setting than much larger resources initially promised and suddenly cut back after implementation has begun.

G. Some PNG Considerations

PNG in 1979 is not Tanzania in 1961 albeit it shares certain characteristics including a very severe shortage of citizen personnel with civil service or managerial training or experience and a limited set of relevant institutions and policies. One of its potential advantages is the international setting less hostile and sceptical to peripheral economy acquisition and operation of productive enterprises, a second its partially related experience in respect of mining strategy determination and negotiation, a third a more advanced and articulated planning apparatus and a fourth the possibility of benefitting from Tanzanian (and other peripheral economy) experience.

Strategic Choices

Three strategic choices will directly influence the appropriate initial nature and scope of state trading even though each is considerably wider and unlikely to be taken on state trading grounds:

1. continuation of a relatively free trading approach or a (presumably selective) use of tariff or non-tariff protection to increase self reliance in widely consumed

foodstuffs and manufactures. The latter decision would increase the importance of domestic wholesale and distribution channels unlikely to be provided by the existing trading houses and might also justify taking over imports of the items in question to limit destructive competition;

2. the degree to which state (or provincial or local governmental) owned enterprise is to become a central structural element and in particular whether finance and foreign trade are to become dominantly in the state sector to implement resource (foreign exchange, surplus, credit) allocation. A decision to pursue a public enterprise centered approach over a brief time period would necessitate rapid buildup of state trading centered on import/export operations and at the same time would maximize total enterprise sector personnel and public institution requirements;
3. whether PNG is to embark on a transition to socialism and, if so, what are perceived as the key obstacles and forms of exploitation to be overcome.

Import/Wholesale

Subject to the previous notes on impact of strategic decisions, the general impact and wholesale business would appear to be the most promising point for instituting state trading. The range of activities would include collection of data on demand, purchasing, importing and central warehousing, distribution to provincial (at regional) warehouses, wholesaling.

Initial entry into specialised goods - eg vehicles or mining equipment - is probably unwise. So- barring a decision to embark on a speedy transition to socialism - is an immediate takeover of all general importing (let alone all wholesaling). However, consideration should be given to taking over 100% of certain major imports eg sugar, flour, beer, cigarettes, galvanised sheet, cement, dairy products - as soon as capacity to handle them is created or acquired. (Confinements for goods not actually handled should be avoided if possible). Similarly sole power - and duty - to import should be given in respect of goods (eg potentially dairy products, fresh meat) in respect of which major attempts to achieve national self sufficiency are being made and a priority duty of the storage, distribution, wholesale functions should be to handle the domestic product effectively. (If other wholesalers wish to handle it and/or the production units can distribute directly there is no self evident case for

giving the general import/wholesale Company a monopoly on the domestic product but it will then need to co-ordinate to avoid swamping or starving the market by faulty import decisions).

Once the state trading unit is successfully established with - say - a quarter of the general impact trade (perhaps 10.15% of total imports), consideration will be needed as to whether it should be expanded to a dominant position in respect to general imports and whether it should extend its coverage to more specialised times. At the same time consideration of structure - eg three or four specialised importing companies with central storage and limited wholesaling functions, four to six general required wholesale enterprises (eg Port Moresby, Gazelle, Bougainville, North East, Northern Highlands, Southern Highlands) and a Board of Trade to perform sectoral planning, training, coordination and regulation functions - should be carried out.

Initial management poses problems. The simplest route - creating a joint venture or a 100% takeover plus management contract - with a present major private importer would create a viable trading enterprise with an experienced management. Whether it would really increase PNG central over trading or provide a vehicle for broader change is quite another matter - probably not without major government attention and a subsequent management change.



Building up a new venture from scratch with self management (including individually hired expatriates) would be slow, risky and demanding a degree and type of government supervision which is probably not available. To a lesser extent the same would hold for a new company with a management contract with a firm not previously active in the South Pacific region.

A possible compromise approach would include:

- a. acquisition of one large importer/wholesaler;
- b. retention of its citizen staff and - on secondment - selected experienced expatriates;
- c. Contracting with the Scandinavian Wholesale Co-operative Federation of Copenhagen (an import-wholesale venture of the national nordic co-op federations) for a senior management team (including purchasing expertise) and a citizen staff development programme;
- d. creating a state tradeliason unit in Planning or Commerce to work closely with the new enterprise to build up government expertise and to identify problems for trading well before they reach crisis level. As a base for a subsequent Board of Trade this unit must include senior appropriately trained PNG officials not expatriate advisers and standard PNG civil administrators only.

If this approach is adopted the Scandinavian Federation or one of the national federations could be approached in respect of a pre-establishment consultancy team to work with a PNG Task Force. Alternatively CFTC might be

approached for a Commonwealth team.

PNG already has a public enterprise involvement in respect of commodity exports which it may wish to expand. The presumptive reason would be attaining better prices which requires either access to major world market price data virtually on a daily basis or contracts with buyers linked to world market prices on delivery date and requiring supply of proof of stated price. The data - for some commodity - can be served from the Reuters Commodity Service (telex) and for others could probably be purchased (and telexed) from selected trading or information firms in Australia, Japan, the USA (preferably West Coast for PNG), the UK, the Netherlands and Federal Germany.

Initially specialisation in two or three crops - eg coconut products, coffee, timber - would seem desirable to limit the amount of knowledge and range of market patterns. Information on state trading in some of these products (eg timber in Malaysia, coconut products in Sri Lanka, coffee in Tanzania) can probably be secured by CFTC. PNG is not a large enough producer for either local auctions or multiple overseas offices to be commercially practicable. Negotiation of relatively large contracts with users - oil millers, soap makers, edible coconut products wholesalers, timber wholesalers - or use of selected traders (with regular checking of price received against market data) would, on the face of it, appear the most practical approaches.

Again an initial senior management team would be needed. The Scandinavian Wholesale Co-op Federation would again be a potential source - seconded employees could in this case be counted upon not to sell at special prices to their permanent employer which is a substantial buyer of several of these items though not currently from PNG. Alternatively a middle sized broking house might be interested in a minority stake in a joint venture and so long as clear barriers to its selling to itself were maintained this might be a viable initial approach. Identifying such a firm would pose problems and require specialist advice.

Copper presents different issues. A PNG state trading enterprise acting as sole seller - on the lines of Zambia's Memaco - could raise the total foreign exchange receipts if it operated effectively. CFTC could secure detailed advice based on Zambian and Chilean (pre 1973) experience. However, so long as copper is exported as mixed concentrate and not as blister or refined it is doubtful that the expertise to run such a sale marketing company could be secured. That is an additional revision for pressing ahead with securing local smelting (blister) for Bougainville and possibly local refining when the second mine is in production.

Subwholesaling, Retailing and Export Collection

Subwholesaling and retailing are not very suitable sub-sectors for a national state trading venture. Whether they are priority areas for action in PNG is a different question.

Up-country shops - PNG national owned private or village co-ops - could be helped by provincial and required wholesale depots and (possibly) further transporting by a state trading enterprise. A programme for training managers and bookkeepers could be run by the state trading company on a contract from the government or as a part of a co-operative development programme.

In respect to urban trade, the key question is whether it is reasonably efficient and has reasonably acceptable profit margins. If yes, a moderately low key training programme for a limited number of consumer co-op personnel may be adequate. If not a small number of retail outlets in major towns could be handled by the import/wholesale corporation and retail price control based on its wholesale prices established and enforced (at least as long as there were no major physical shortages).

Whether domestic food export crop collection is a priority area for state trading depends on the adequacy and cost of existing collection structures. A case for the export corporation opening purchase depots in main producing areas and for the import/wholesale unit doing likewise for selected products (eg. meat,

dairy products) can be made. Similarly, for smallholder (peasant) production, co-operative supply of inputs and seasonal credits initial purchasing, bulking up, initial storage would appear likely to be economically and technically viable and consistent with PNGs political economic strategy. However, such developments - especially for the village co-ops - require careful personnel training (short courses for village members plus perhaps accountants and technical advisers serving groups of co-operatives) at the initiation of the programme. The village co-op operation is unlikely to be successful without prior provision of state trading unit buying (and possibly agricultural input and implement selling) depots and arrangements for provision of seasonal credit, advisers/inspectors and technical support.

### Provincial Enterprises

Neither the import nor the export field appears appropriate for provincial state trading. The expertise and volume requirements on the one hand and the relationship to specifically national goods on the other lead to this conclusion.

Wholesaling, in principle, may be different. However, at present at most three provinces (Port Moresby, Bougainville, Gazelle) would seem likely to be able to create economic enterprises with any substantial degree of provincial personnel input on control. Even in their cases it is probable

that such a venture would be premature.

If it is desired to provincialise state trading at whole-sale level, then this could be kept in mind in organising the systems and structural patterns of an initially national company. Then after two to five years experience a deliberate provincialisation (or regionalisation for the provinces with the smallest turnover and personnel availability) programmes could be set up while retaining supervisory and coordinating powers plus training and backing managerial support with a national Board of Trade.

Retailing is almost certainly unsuitable for regional operation. Village or urban neighbourhood co-operatives are much less unlikely to be efficient albeit, as noted earlier, their building is likely to be a lengthy and tedious process.

### Prices and Margins

State trading should not raise general consumer prices above or reduce general producer prices below what they otherwise would be. (Taxation is a more appropriate instrument). Assuming care is taken to avoid excess costs (eg. too many senior personnel, too high stocks, too many bad debts, poor purchasing or selling) there is no reason to assume it will have that effect. Indeed, to the extent that it increases competition for previous

oligopolists and/or improves up-country distribution/collection, it should affect consumer and grower prices positively.

Beyond that caution is needed:

1. Pan-provincial (main wholesale depot at major centre retail) price equalisation should be introduced selectively and with care to avoid losses on distant sales centres not offset by gains on sales real import or production points;
2. initial margins should be set to allow a surplus on fairly cautious assumptions as to turnover and costs (subject to the constraint of rarely and marginally raising the price above the previous private sector level!) - it is better to be able to cut them later than to face the need for a margin and price raising exercise to escape from a sea of red ink and subsidies;
3. price control is probably better handled by a separate quasi independent body - with its own data collection powers and analysts responsible to a Commissioner perhaps with a board representative of consumers, producers, workers and political parties - than by a state trading enterprise whose margins and

State trading can limit profit margins and sometimes purchase/sell at prices more nationally advantageous than private enterprise. It can be a tool of managing price movements. However, the degree to which it can reduce consumer prices (especially in an inflationary world) is usually limited. In the absence of concrete data on why PNG or some provinces, are exceptions it would be imprudent to make larger claims in this respect or to seek to implement them without regard to financial viability. To do so would create an area of failure and distract attention from what state trading actually can achieve.

#### H. Concluding Note

This paper does not argue whether or not PNG should decide to embark on state trading. That is a decision for PNG decision takes responsible to the people of PNG to make. It does seek to set out what state trading can achieve as illustrated by its research in a somewhat similar state - Tanzania - are the past two decades. This may help inform them who must advise PNG decision takers and allow a decision based on broader knowledge than would otherwise be available.

Nor does it seek to structure state trading for PNG. In part that too requires political decisions. Further it requires detailed knowledge of PNG public sector resources,



surplus generating capacity are themselves major concerns in respect to price determination. Implementation assistance - informing retailers of approved prices, cutting supplies to profiteers, supporting co-ops - can be assisted by state trading ventures but to give them central price setting powers is to create a built in conflict of interest situation.

priorities and constraints and of the political economic context of PNG, best supplied by PNG officials (citizen or experienced expatriate). Finally it is desirable that specific venture creation be based on detailed feasibility studies of that venture which can be done only after initial political and broad technical decisions. Again the Tanzanian experience may offer useful guidelines, comparisons and approaches to use, adapt (or avoid!)

However, in general it seems fair to say that state trading can be useful to most peripheral economies. This is especially true for those committed to reduction of inequality, increased self reliance and reducing dependence on foreign and domestic minority community capitalists. On that basis, it would appear reasonable to suppose that state trading can play a positive and growing role in the development of Papua New Guinea by and for Papua New Guinean workers and peasants.

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