Post-privatisation changes in management control, firm activities and performance

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8 Conclusions and implications

8.1 Objectives and research method

This research study has investigated the changes in the MCS practices, activities and performance of three firms in a developing country. It was based on the following central research question: *'How do internal and external factors affect the relations among privatisation, MCS change and firm performance?'* The research was conducted in Eritrea. Its main objective was to gain insight into the process of change induced by the privatisation of Eritrean businesses. To make our analysis more extensive we took into account the influence of both internal and external contextual factors. The study particularly focussed on the role of the government in the privatisation process and the question whether it offered the Eritrean firms sufficient support to privatise successfully during the transition period. In addition, an attempt was made to develop a conceptual framework that can serve as a basic model for conducting research in LDCs.

In order to perform an in-depth analysis we chose a qualitative research approach combined with the case study method. In this way we could collect a rich spectrum of data that enabled us to make a thorough and reliable description and analysis of our research topic.

8.2 Theoretical arguments and expectations

The first three chapters of this thesis discussed the necessity of privatisation for LDCs, while including the influence of internal as well as external contextual factors. Privatisation has generally been regarded as the solution to the failure of public ownership (Shirley & Walsh, 2001). Public ownership has a number of disadvantages. *First*, public firms are protected by the government and face no market pressure (competition). They are dependent on subsidies, which makes them inefficient (Lieberman, 1993). *Second*, public firms are not focussed on profitability. They are in the first place aimed at performing welfare functions (Young, 1995). In addition, there is a great deal of political interference in the appointment of the managers of public firms (Kumar, 2004). Further, an important objective of public firms is to reduce unemployment. *Third*, the degree of interference of government bodies in the firms' daily affairs is high, resulting in overstaffing, bad product choices, a lack of investment measures, and poor incentives for managers (Shleifer & Vishney, 1994: cited in LaPorta & Lopez-de-Silanes, 1997). The principal (owner: the government) has less knowledge of the firm than the agents (the managers), which causes information asymmetry, making it difficult to monitor the agents' behaviour and performance. Due to the long chain of principal-agent relationships, the control process in public firms is weak. In addition, due to the bureaucratic structure of their decision-making process public firms are not capable of responding to market developments in a timely manner (Vickers & Yarrow, 1988). For these reasons the performance of public firms is often poor.

Privatisation was expected to improve the public firms' efficiency in LDCs in various ways. Moreover, it would give the owners the right to appropriate their returns for assets, and to introduce incentives (Hart & Moore, 1990; Hart, 1990). Further, privatisation was believed to encourage measures of innovation and stimulate the productivity of LDC firms (Erbetta & Fraquelli, 2002). In addition, the public finance difficulties were expected to be resolved by the market mechanism (Cook & Kirkpatrick, 1988). Competition and the transfer of property rights into private hands was considered to improve the MCS, including the accounting systems (Macias, 2002), as well as firm performance (Vickers & Yarrow, 1988) and to stimulate development goals (Rees, 1985). As privately owned firms operate in a capital market governed by the profitability principle, managerial non-profit behaviour is limited (Ott & Hartley, 1991). Studies claim that privatisation has resulted in higher outputs, an increase in investments, the production of quality goods and services at low prices, the introduction of modern technology and know-how, and efficiency improvements in firms' corporate governance. The salaries of employees in private firms are higher, whereas the leverage is lower, and the government benefits from the increase in taxation income (see Makalou, 1999; Fahy, *et al.*, 1999; Kikeri *et al.*, 1992). It was assumed that the post-privatisation MCS practices would be advantageous to the LDCs in the following ways. *First*, the newly introduced MCS practices would be less bureaucratic and more profit-oriented, thereby contributing to the economic welfare of the firms (Uddin, 1997; Waters, 1985). *Second,* they would be closely associated with economic rewards and a more efficient allocation of resources, combined with new initiatives, such as total quality management and improved employee benefits. *Third*, they would focus on market information. Post-privatisation MCS practices were increasingly linked to the developments in information technology, as a result of which they had become more and more transparent. *Fourth,* politics and bureaucracy played no role in post-privatisation MCS-practices. They were incentive-based and supported through market-driven budgets. *Finally*, they would require the participation of both managers and employees, thereby ensuring a thorough and reliable control process (Uddin & Hopper, 2003, 1999).

Both a successful implementation of MCS and an increase in firm performance levels are related to internal and external contextual factors. External contextual factors are market and country conditions (DeCastro & Uhlenbruck, 1997), entailing government regulations, the political climate, industrial relations (TU), the influence of aid agencies, and competition (Kennedy & Hobohm, 1999; Hoque & Hopper, 1997, 1994). The literature indicates that it is mostly the large Western firms that make use of modernised and improved MCS, and that their usage requires the noninterference of the state in the firm's management, the presence of efficient capital markets, a transparent structure of the firm's management and control practices, and an unlimited access to capital. Unfortunately, these conditions are often absent in LDCS, which undermines the development and success of the private sector. Most privatised LDC firms have no access to resources and support services. Their operations are hampered by harsh governmental regulations on foreign trade, the abolishment of forex services, excessive borrowing by the government, heavy taxation, and socio-political instability. So in order for the private sector to operate successfully a favourable business environment is required (Kennedy & Hobohm, 1999). Some post-privatisation studies indicate that privatised LDC firms have adopted informal control systems that are different from those used by Western companies (see Hopper *et al.*, 2004b; Uddin & Hopper, 2003, 1999).

Internal contextual factors include firm size, the organization's capacity to learn and act, the introduction of new technology, and strategy changes. Empirical evidence shows that the management control systems of firms that have formed alliances with multinationals or other large companies are usually more sophisticated than those used by firms owned by locals (Al-Namri, 1993). The latter are inclined to make less use of MCS techniques than the larger firms (Chiu, 1973; Savage, 1966: cited in El-Ebaishi *et al.*, 2003), since their financial resources are relatively limited (Libby & Waterhous, 1996). Because of their size the smaller firms can use control systems that are more informal, such as direct control exercised by the owner(s). The renewal of a firm's management control systems is connected with the skills of its staff members (Cohn & Levinthal, 1991), a firm's capability to provide its staff members with training, or its decision to hire experienced personnel (Firth, 1996). Bruns & Kaplan (1987) argue that the support and involvement of firm owners as well as top-managers facilitates the introduction of MCS changes and innovations.

8.3 The case firms under public ownership

During the public ownership era, the three case firms (IMA, AW&LF and RSBSC) as well as the other firms in Eritrea stood under the supervision of the public corporations and the MTI. All plans and strategies of the firms were centralised, which meant that there was a great deal of governmental interference. This clearly undermined the firms' autonomy. In addition, the long chain of bureaucracy and the inherent information asymmetry affected the decision-making processes of the businesses in an unfavourable manner. Firms were expected to limit their production output to predetermined quotas and adopt fixed salary scales. The role of the managers was restricted to the execution of the plans formulated by the governmental bodies. Moreover, these managers were in fact appointed by these institutions, and lacked skills and authority. During this period the markets were protected, and therefore there was no competition. Budgeting policies were just a formality, requiring the firms to prepare statistical reports each quarter and financial statements each year, although no feedback was given on these reports. During that time management information was used poorly; it was merely subservient to financial accounting. Firms had no clear strategy and neither did they have long-term plans. In addition, training facilities for employees did not exist. The employees had no real sense of responsibility or commitment. Moreover, the firms' products were of poor quality, partly resulting from the fact that the government did not allow them to make investments in new machinery and equipment. Further, the poor state of the public firms' machinery also undermined their efficiency, productivity, waste management, and competitiveness. On top of that, their labour force was needlessly large, and through their access to bank overdraft facilities they were heavily indebted. All in all, the public firms had no profitability drive.

8.4 The effects of privatisation

8.4.1 New ownership:

The new owners of the privatised firms had a different background than the former ones. For example, IMA's owner lived in Europe, from where he ran a retail business. Although he had received no accounting or management training, he was an experienced retail business man and possessed knowledge of the European market. He was IMA's manager and assisted the firm in importing raw materials and penetrating the export market. The owners of AW&LF were Eritrean. They had a technical background, but no training in accounting or management. They were, however, very motivated to gain knowledge about accounting practices, and they frequently conducted market surveys to assess the possibilities of expanding their market share. RSBSC was a joint venture between the GOE and CCC. The company was governed by a Board of Directors and the staff members who held key positions were qualified people. The manager was a chemist by profession and had gained a lot of experience from 1991 onwards. The owners of both IMA and CCC offered the joint venture assistance in the import of materials. In addition, RSBSC gained access to CCC's knowledge. In general, the activities of the owners of all three case firms were clearly focussed on realising the business and investment plans.

8.4.2 General changes:

This section discusses and compares the changes in terms of investments, product market decisions, employment, raw material sources, the employees' mentality, and organizational structure. The case firms accomplished the following goals. *First*, privatisation restored firm autonomy and stimulated new investments. In this way old machinery could be renewed or replaced. This generally meant the automation and computerisation of production and business processes, which led to a higher productivity, better product quality, and less wastage. Further measures included the provision of employee training, expanding the production capacity and sales activities, the purchase of delivery trucks by AW&LF and RSBSC, and the introduction of accounting facilities (computer software). The CES and CEA ratios presented in tables 5.1, 6.1, and 7.1 show the impact of the investments made. In addition, the investments reduced the firms' leverage ratios. High leverage ratios as a result of public financing had been a burden to the companies during the public ownership period. The relief from this burden was one of the effects of privatisation (Cook & Kirkpatrick, 1988). In general we can conclude that the increase in post-privatisation investments is in line with the theoretical expectations as presented earlier. *Second*, privatisation resulted in the introduction of new products and the expansion of markets to enhance profits. So we observe that all firms achieved success in terms of increasing their sales growth, labour productivity, and operational efficiency (as measured by sales per employee). In the case of AW&LF, however, sales growth slowed down at a certain point. IMA shows mixed figures with respect to sales growth; in some of the post-privatisation years the figures were lower than in the base year. Apart from that, the firms positively contributed to the government income by paying higher amounts of tax than in the public ownership period. In terms of ROS, ROA, and ROE figures, however, all three firms show poor profitability results. In addition, their net income efficiency did not improve after they were privatised. This can mainly be explained by the influence of the contextual factors. *Third*, the firms started to adopt clear strategies with respect to product pricing, product types, and markets to operate in. These new strategies emphasised quality, customer satisfaction as well as higher productivity and return levels. *Fourth*, privatisation changed the employees' working mentality; they became more committed, more productive, more duty-conscious, and more responsible. For a summary of the post-privatisation developments after the privatisation of the case firms, see Appendix-D.

Differences: There were also differences among the case firms in the implementation of their business and investment plans. *First*, RSBSC improved its workforce in terms of both quality (by the provision of training) and quantity (by hiring qualified employees, both at the higher as well as the lower posts). This was made possible through the assistance of CCC and the installation of a new bottling line, which had a larger capacity. In addition, the firm's lay-out was adapted to Western standards. At RSBSC, both the employees' salaries and benefits were considerably higher than those at the other two case firms, resulting in a highly motivated and satisfied workforce. RSBSC's policy was to upgrade the salaries on an annual basis and to compensate its employees for inflation. In addition, employees who performed well were rewarded. With respect to the size of the workforce, IMA and AW&LF showed a decline in manpower after they were privatised, which is in line with findings of other studies (e.g., Aussenegg & Jelic, 2002; Harper, 2001; D'Souza & Megginson, 1998). These findings are not surprising; during the public ownership period the size of the workforce had become needlessly large, so the superfluous employees were made redundant. Unlike RSBSC, IMA and AW&LF were not in the position to offer their employees salary increases or to introduce incentive systems. Moreover, the activities of the two firms clearly suffered from contextual factors. Further, with respect to hiring skilled manpower costs were no issue to RSBSC, and decisions about personnel were not influenced by family ties. This is why RSBSC could appoint fresh talent with proper skills at key positions, thereby increasing its chances to improve its performance (Ramaswamy & Von Glinow, 2000). IMA and AW&LF, on the other hand, were limited to appointing friends and/or family members at management positions (GM, Production Department), because their main criterion for hiring staff was trust. Another reason was the lack of skilled labour in the market.

Second, RSBSC's firm performance and output figures were favourable, but those of IMA and AW&LF were mixed. The fluctuations in these companies' figures were the result of the lack of labour and forex since 2001. *Third,* IMA's production capacity largely extended the demand of the home market, which is why it aimed at exporting the majority of its products. The export market was large and quality-oriented, and required a timely and fixed delivery of goods. Further, products could be offered at higher prices. RSBSC's Sales Department was unique; it was highly organised, operating with a large number of sales agents and some market developers. It also had a large number of delivery trucks at its disposal. In addition, it provided the outlets with various kinds of support. The department was fully supported by CCC. It can be observed that the experience and knowledge of both IMA's owners and those of CCC contributed in expanding the market successfully. Locally, IMA as well as AW&LF were challenged by the activities of competitors, the import of cheap foreign products, and customer preferences. The local competitors sold their products cheaper, and the customers preferred these cheaper products, even though they were of lesser quality. In addition, IMA's local trade activities were undermined by the governmental decision to import similar products rather than to buy them locally. Similarly, as market surveys indicated, local customers preferred imported to local wines because they considered foreign beverages to be of higher quality. This in particular hindered the activities of AW&LF. RSBSC did not face problems of this kind, since it had a monopoly position in a market that was still unsatisfied. *Finally*, the three firms varied in their measures with regard to the improvement of their organizational structure. RSBSC invested in the expansion of its departments, and formulated clear business plans and job descriptions. In addition, its GM was given more autonomy. In the case of AW&LF the owners had the power of decision-making and were closely involved in the day-to-day activities of the firm. IMA's organizational structure was simplified. Here, family members played a key role in the management of the firm besides the owners.

8.4.3 Changes in MCS practices and firm performance

Planning and budgeting: After the case firms' privatisation their planning and budgeting practices changed. IMA abolished its formal planning and budgeting procedures and introduced short-term plans based on customer orders. The reason for this was that its owners did not support long-term measures, mainly because they lacked sufficient knowledge of market demand issues. Moreover, there was a shortage of accounting staff. Also AW&LF did not prepare formal budgets, but made annual sales plans on which it based its activities. However, these plans were neither used for control purposes nor did they serve as criteria for the achievement of goals. The company's production was targeted at replenishing the stock, and it made sure it had an extra wine supply in the case of any unforeseen demand, which was necessary since the process to manufacture wine took several weeks. The materials stock was checked each month to facilitate a good purchase policy. The reasons of AW&LF for not carrying out budgeting practices were similar to those of IMA. Also AW&LF was challenged by a fierce competition, a shortage of empty bottles, and forex problems. Further, both firms dealt with a lack of managerial knowledge, ability and experience. These restrictions together with cost issues blocked the introduction of significant changes in the firms' MCS practices (Libby & Waterhouse, 1996). The restricted use of formal MCS tools at both IMA and AW&LF is in line with the theoretical argument that small firms are not particularly focussed on formal MCS techniques and procedures (Chiu, 1973; Savage, 1966: cited in El-Ebaishi et al., 2003). The firms' lack of managerial skills and experience corresponds to the findings of case studies conducted in Bangladesh and Sri Lanka (Hopper et al., 2004a). In general it can be concluded that IMA and AW&LF adopted a short-term planning and control approach based on a short-term market demand and aimed at day-to-day activities, which were directly monitored by the managers.

RSBSC, on the other hand, conducted both long- and short-term planning and budgeting activities. Market demand was forecasted on a regular basis, past sales trends were analysed, and the Production Department was provided with detailed product line information for planning purposes. In addition, in the case of changes in the inventory or in the sales movements of the product lines, the production plan was adjusted. In general, the budgeting procedures were based on the company's strategic plan. The lower departmental levels also participated in the budgeting process. As a result the firm's budgeting policies became more realistic and effective, giving a clear direction to the departmental activities. This outcome is similar to the findings of studies conducted in Indian firms (see Anderson & Lanen, 1999). The improvements in RSBSC's MCS were in fact initiated by CCC. As indicated by Al-Namri (1993), the MCS techniques adopted in joint ventures are generally more comprehensive and sophisticated than those used in small local firms. RSBSC's MCS was clearly more formal and structured, and can be classified as a combination of a diagnostic and a belief system (see Simons, 1995). So the post-privatisation MCS developments that took place within RSBSC are consistent with the theoretical expectations presented earlier.

Product costing and pricing: All case-firms used standard costing methods and possessed knowledge of input-output relationships. In the case of IMA, however, the overhead costs included personal expenses. Although the three case-firms did not use advanced costing methods, such as activity-based costing, RSBSC made an attempt to differentiate the costs of each activity for control purposes. In the case of AW&LF, product costing was affected by the integration of the office building depreciation costs into the manufacturing costs, which made the figures unreliable. IMA and RSBSC classified their costs in an adequate manner.

The firms varied in setting their product prices. With respect to the export market, IMA was free in setting its prices, but in the local market it was forced to apply moderate price levels for competitive reasons. To attract its clients IMA offered quantity discounts and emphasised the high quality of its products. AW&LF was a price taker, since its competitors offered their products at lower prices. Both IMA's and AW&LF's commitment to maintaining a standard quality for input as well as output limited their price flexibility and made it difficult for them to compete in the home market. RSBSC adopted fixed product prices, because their customers could not afford to pay higher prices. In general, we can observe that the prices of raw material input were continuously rising due to inflation and changes in the import-export regulations. RSBSC, on the other hand, benefited from the input discounts offered by CCC whenever the firm's profitability was impaired by external influences.

Internal reporting and decision-making: We observed the following *similarities* among the case firms. All three firms continued most of the reporting procedures introduced in the public ownership period, and made additions and/or improvements if necessary. After the firms' privatisation the reports and analyses became more sophisticated and detailed, and they were used for monitoring purposes, which had not been the case in the public ownership period. With respect to internal reporting and decision-making privatisation brought clear improvements and benefits. In addition, the firms introduced the use of non-financial information to improve their product quality and design and to increase their insight into the performance of competitors.

Differences: *First*, IMA partly abolished the formal reports, and replaced them by personal supervision. This measure was taken because of the reduction in the organization's size and the lack of interest on the part of the owners to receive detailed formal reports. In fact, the firm operated as a small shop, where personal supervision played a major role. Only short-term reports, such as the daily production report, were used. *Second*, IMA and RSBSC were clearly more focussed on daily reports than AW&LF. This was because the owners of IMA and RSBSC were not physically present in the firms, and these reports provided them with information on the companies' day-to-day activities. In general, automation and computerisation improved the standard and frequency of the reporting procedures to some extent. However, especially at IMA and AW&LF, further developments were hampered due to cost considerations. This did not apply to RSBSC; with respect to the introduction of innovations and investments in the field of MCS, its owners (i.e., CCC) were in the position to provide the company with means and know-how as well as financial support. Both CCC and the owners of AW&LF encouraged the effective use of reports. The accounting staff of RSBSC and AW&LF was therefore relatively larger than that of IMA.

Third, our findings indicate that RSBSC was the first to computerise its accounting procedures and establish a network connection between the departments. In addition, a QC Department was set up. In 2004 IMA and AW&LF introduced computers in their Finance Departments. The firms mainly computerised their financial reporting tasks. Due to the limited number of skilled employees the computerisation could not be extended to other areas. Moreover, in the case of IMA the manager's power was weakened by a family member. At AW&LF the shareholders shared the decision-making power. In the case of RSBSC all departments possessed the autonomy to make decisions, the BOD being the highest decision-making body. We can conclude that initially privatisation stimulated a more efficient and effective decision-making process and facilitated the modernisation of certain business procedures. In addition, privatisation increased the involvement and interest of the owners in their businesses.

Cost control and waste minimisation: The following similarities among the firms can be observed. They all committed themselves to improve the quality of their products. The process of quality checking started with the purchase of raw materials and continued until the end products were delivered to the customers. The owners were closely involved in this process. The standard input-output relations were used to control the resource consumption. All steps of the production process were meticulously checked, and if there were any anomalies, direct action were taken. The employees' mentality had clearly changed: they had become committed and quality-conscious. All three firms were aimed at working efficiently, increasing their productivity, and reducing their wastage. RSBSC and IMA introduced computerised new machinery, while AW&LF renewed its machinery and built new stores. All in all it can be concluded that privatisation improved the firms' quality standards, cost-consciousness, and waste minimisation, and that it strengthened their competitiveness.

Differences: *First,* RSBSC reduced the issue of bottle and crate breakage by establishing a 'Breakage and Sanitation Committee' as well as conducting regular checks. Further, it was able to control its costs by computing them separately, that is for each activity. *Second*, in the case of RSBSC, the joint-venture with CCC paved the way for the implementation of a quality system and improvements in the operating procedures. This is an example of the benefits that a strategic alliance can bring in terms of MCS improvements introduced by an international firm, as indicated by Firth (1996). This evidence also supports former research findings gathered in Syria (Abdeen, 1980) and China (Chan & Lee, 1997), which show that some Western accounting concepts are indeed applicable in and beneficial to LDC firms. Furthermore, our results are in line with the views of Bruns & Kaplan (1987), who state that the support and participation of companies' owners and top-management is vital for the realisation of MSC change in business firms. *Finally*, CCC conducted its own quality checks by taking random samples from the market on a monthly basis.

***Performance measurement and evaluation*:** After the three case firms were privatised they started to conduct similar activities in the field of performance measurement and evaluation. Either directly or indirectly, they collected non-financial information from clients. In addition, they became more focussed on both customer satisfaction and profitability. All of them monitored their production daily, controlled their resource consumption, and frequently had supervisors monitor their activities. They used their daily, weekly and monthly reports effectively for control purposes. In this way all steps of the production process could be identified, making it easy to detect any possible delays.

Differences: *First*, with respect to managing its activities and the measurement and evaluation of performance RSBSC had access to the knowledge and experience of CCC. In controlling the firm's actual performance, the standard yields of sugar and concentrate were used as a basis. *Second*, both RSBSC and IMA constantly evaluated the performance of their employees, which was laid down in formal reports. In the case of RSBSC, these evaluations served as guidelines with respect to promotions and bonus payments. AW&LF, however, did not evaluate individual performance, since it was merely focussed on the firm's productivity as a whole. This was because the firm's shareholders were in fact physically present in the departments, which was not the case with the other firms. *Third*, IMA's control activities were hampered by familial ties similar to those reported by Uddin and Hopper (1999), who argue that a structure consisting of family members at top managerial positions weakens the authority and control practices of both middle management and the hired managers. *Fourth*, neither IMA nor AW&LF used formal budgeting tools for control purposes, which is in line with the findings of Hopper *et al.* (2004b), who observed the preference for informal ways of control to formal budgetary control systems after the introduction of privatisation. *Finally,* RSBSC's daily sales reports were very detailed, classifying the firm's sales by means of area, product line, and type of outlet. This approach enabled the company to exercise control at all levels.

In brief, after privatisation RSBSC's MCS practices became proactive in the sense that they helped the firm identify threats and opportunities (by means of market surveys and performance evaluation reports) in order to achieve its primary goal, namely improving its future performance. After privatisation, RSBSC's MCS, which formerly could be typified as consisting of diagnostic methods, developed into more structured, direct and explicit systems, whereas the MCS of IMA and AW&LF became largely implicit. The MCS of the latter two companies could in fact be considered as a mixture of diagnostic and belief systems. Although both firms did not prepare formal budgets, they did formulate short-term production plans. In addition, both firms applied standard costing, measured their resource consumption, monitored their production, and tried to reduce costs and wastage. They succeeded in reducing the amount of paperwork considerably. Their MCS clearly became more cost-effective and efficient. IMA and AW&LF also became focussed on improving the quality of their products and workforce. Advising and training their employees regularly was an important issue. The firms did not have a formal incentive system as used by RSBSC. Instead they tried to motivate their employees by offering them salary adjustments to support them in dealing with the unfavourable economic situation. The discussions in the chapters about the individual firms indicate that after privatisation the owners became heavily involved in the companies' internal matters. So the owners' interest and capability played a vital role in the process of MCS change. For a summary of the case firms' post-privatisation MCS practices, see table 8.1. For a more detailed review of post-privatisation MCS changes and developments, see the appendix section (Appendix-D).

Table 8.1 *Summary of post-privatisation MCS practices at case firms.*

Firms / MCS Techniques	IMA	AW&LF	RSBSC
Planning & Budgeting	- Short-term, demand oriented - No budgeting practices - Impact of capacity utilisation and uncertainty	- Short-term, focus on replenishing inventory - No budgeting practices - Impact of uncertainty and competition	- Both short and long-term orientation - Regular budgeting & strategic plan - Large capacity and size, support of owners and computer facilities - Regular meetings and follow-ups
Internal reporting & Decision-making	- High interest and usage of reports - Finance department is weak and heavily overloaded - Limited usage of computers - Decisions are shared and fast	- High interest but moderate usage of reports - Finance department is a bit slow and few people operate activities - Limited usage of computers - Fast decision-making process	- High interest and frequent usage of various internal reports - Strong and fast Finance Department with qualified personnel and facilities - High usage of computers and soft-wares - Fast decision-making process
Product costing & Pricing	- Knowledge of standard costs, input-output - external and internal factors affect costs - Price taker at home market but free on export pricing	- Knowledge of standard costs, input-output - external factors affect costs - Price taker at home market	- Knowledge of standard costs, input-output - external factors affect costs - Fixed pricing policy for wholesale and retail activities
Cost control & Waste minimization	- Strict quality control [QC] at each production step - Trained QC staff, employees, and role of automation	- Strict QC mainly during production process - Renovation of machinery - Construction of stores	- Strict QC on input, throughput, and output and regular monitoring - Role of automation and trained staff - Involvement of CCC - Use of TQM and monitoring committee
Performance measurement & evaluation	- Monitor resource usage, labour productivity, and use of physical supervision - Some usage of non-financial information	- Monitor resource usage, output, and use of physical supervision - Monthly meetings and moderate usage of non-financial information	- Intensive usage of daily reports to monitor activities, rigorous physical supervision, conducts variance analysis - Monthly & quarterly meetings - Intensive usage of non-financial information

***Firm performance*:** When comparing our findings on firm performance (tables 5.1, 6.1 and 7.1) with those of former studies, we can conclude the following. Our results show that during the post-privatisation period the firms' performance generally improved in terms of sales growth. All firms managed to achieve an increase in their sales revenues, although these increases differed per firm. In the case of IMA and AW&LF sales did not increase instantly, whereas RSBSC's sales figures rose significantly during the period under review. Our results are in line with the expectations with respect to the effects of privatisation and correspond to the findings of Megginson *et al.* (1994), Boubakri and Cosset (1998), LaPorta & Lopez-de-Silanes (1997), D'Souza *et al*. (2001), and Frydman *et al*., (1997), which are discussed in chapter three. Profitability as measured by ROS, ROA, and ROE, however, did not improve after privatisation. This finding is consistent with those of Harper (2001) and Aussenegg & Jelic (2002). It is not in line with the theoretical expectations regarding the effects of privatisation, and neither does it correspond to the findings of Boardman and Vining (1989), Megginson *et al.* (1994), Boubakri and Cosset (1998), La Porta & Lopez-de-Silanes (1997), D'Souza *et al.* (2001), Frydman *et al* (1997), and Ramaswamy (2001). The results of our case studies should, however, be interpreted with caution.

All three firms were confronted with unexpected problems resulting from changes in the institutional environment. In addition, our findings indicate that the firms' post-privatisation ROA and ROE figures were affected by the amount of investments made. High investments in fixed assets yielded high depreciation expenses, which had to be weighed against the periodic revenues.

Positive outcomes of privatisation included improvements in productivity and operating efficiency. Also the firms' sales efficiency increased after they had been privatised. Nevertheless, RSBSC's post-privatisation net income efficiency declined, but its output percentages increased. For IMA and AW&LF these figures were mixed. IMA's output improved during 1999 and 2000 and that of AW&LF during 2000 and 2001. After that output declined in comparison with the base year 1997 due to inflation. The investment and leverage ratios results were positive, which is in line with the theoretical expectations. Especially to RSBSC applied that there was an increase in employment that could be associated with measures such as new investments and expansion activities. In all firms the employees' salaries increased after the introduction of privatisation, which corresponds with the findings of Galal *et al*. (1991). With regard to tax payments, we observed that the amounts paid by the firms were significant in proportion to the sales revenues. In addition to the usual taxes, both AW&LF and RSBSC paid excise tax; AW&LF since 1999 and RSBSC since 2001. Compared to the public ownership period, the governments tax earnings increased after the firms were privatised. We can therefore conclude that our post-privatisation case firms contributed to the national income in a positive manner, as expected (Cook & Uchida, 2004). Table 8.2 compares the firms' performance in the post-privatisation period with that during the public ownership period.

Table 8.2 *Comparison of the case firms' performance in the post-privatisation period with that during the former era*:

Tools / Firms	Profit-ability	Labour Product-ivity	Operating efficiency	Output	Employ-ment	Leverage	Capital invest-ment	Taxes
IMA 1995 - 2004	Poor [Sales mixed]	Better	Better	Mixed	Declined until 2005	Reduced	Better	Increased
AW&LF 1993 - 2003	Poor [except sales]	Better	Better	Mixed	Declined	Reduced	Better	Increased
RSBSC 1993 - 2003	Poor [except sales]	Better	Better	Better	Increased	Reduced	Better	Increased

8.5 Developments in the contextual factors

8.5.1 Internal factors:

Firm size: As our findings indicate, the main internal contextual factors that influenced the expected effects of privatisation on our case firms' MCS practices were reduction in firm size, cost considerations, lack of managerial experience, and the discontinuance of particular activities. IMA's measure to cut down its Finance Department made it difficult for the firm to carry out its MCS practices in an effective manner. In addition, it undermined the assignment of tasks, which in turn made it difficult to carry out the routine accounting activities. Moreover, the fact that too little people performed too many tasks caused considerable delays. The introduction of computer software programmes brought some improvement but could not fully solve the accounting problems. Our findings also show that the MCS tools of the smaller firms (IMA and AW&LF), which were less divisionalised, were less sophisticated and formal than those of RSBSC. In addition, IMA's and AW&LF's resources were more limited, and neither did the firms have access to knowledge and experience in the way that RSBSC had. However, because of the limited size of IMA and AW&LF part of the routine internal reports could be replaced by informal direct controls. In the case of AW&LF, for example, the close participation of the owners in the firm's daily affairs reduced the need for and reliance on comprehensive internal reports. It can therefore be concluded that firm size affected the use of internal reports and the reliance on formal sophisticated monitoring systems. In addition, the physical presence of the owners and their active participation in the firms' daily affairs reduced the need for extensive internal reports.

Organizational capacity to learn**:** The literature indicates that both the size of a firm's Accounting Department and the support of top-management as well as of the owners are vital to the facilitation of MCS practice changes. Our research supports this claim by illustrating that RSBSC was indeed in a better position to innovate its MCS than the other case firms were. RSBSC was able to hire personnel that was more qualified, while it was also in the position to offer its staff continuous training to upgrade its knowledge. IMA and AW&LF, on the other hand, could not implement drastic MCS changes, since they were too costly and the firms' accounting staffs were too small. In addition, the owners of the firms lacked sufficient accounting background to recognise the importance of innovating and improving their MCS. And as already argued, it was in particular the owners' knowledge, experience, and interest that determined firms' choices with respect to MCS.

Introduction of new technology**:** Our research shows that IMA and RSBSC modernised their machinery. To both firms applies that the automation of their machinery reduced their waste levels, enhanced the quality of their products and production processes, boosted their productivity, and enabled them to predict the input-output relations as well as the production timing. In particular RSBSC benefited from the bottle count and date coding reports. The company also computed its machine efficiency and line utilisation to monitor the production processes. The introduction of new technology clearly had a favourable impact on the stability of the firms' business processes, which in turn was beneficial to the planning activities. Moreover, the accounting software reduced the burden of having to carry out the accounting tasks manually, and improved the accuracy and timeliness of the reports.

Strategy changes**:** As our study indicates, all case firms became strongly focussed on strategies aimed at quality improvement and diversification. One of those strategies was adding new products to the existing product lines. Further, all firms introduced strict cost control policies and started to adopt strategies pursuing customer satisfaction and market expansion. IMA was unique in the sense that it introduced new cloth designs on both the local and the export market.

Capacity to undertake action**:** Both IMA and AW&LF suffered from a shortage of qualified accounting staff and they lacked the resources to realise major changes in their MCS practices. In addition, we observed that IMA's owners were very much concerned with saving labour costs, while disregarding the importance of detailed accounting reports. The cost issue made them reluctant to appoint new accounting personnel. Furthermore, the fact that family members had the highest positions in the firm undermined the authority of the hired managers. In the case of RSBSC, radical MCS changes did take place. In this respect RSBSC benefited from the support and commitment of CCC, who gave the company full access to its knowledge, experience, and resources. CCC also succeeded in conveying its mentality and business ethics to RSBSC. In sum, the strategic alliance with a multinational brought great advantages to RSBSC, enabling the firm to make use of an abundance of resources and experience and realise a significant improvement of its MCS practices. In this sense RSBSC can be regarded as a standard example of a firm that fully benefited from its privatisation.

8.5.2 External factors:

When looking at the list of external factors presented in table 2.1, we see that *Culture, Race* and *Ethnicity* are less relevant in the context of Eritrean firms. As indicated in chapter 1, Eritrea has always been a trading nation where many colonial factories are located. This has resulted in a multi-cultural and -racial workforce, which gained a great deal of knowledge and experience over the years, in both manufacturing and non-manufacturing firms. So we did not encounter any significant culturally-, racially-, or ethnically-based elements that had an influence on the Eritrean firms' MCS practices. For examples of the effects of such elements on firms' MCS practices, see the study of Wickramasinghe and Hopper about Sri Lankan companies (Wickramasinghe & Hopper, 2005). We therefore dropped those factors as well as *Aid Agencies* and *Trade Unions (TU)*, since also these latter two played no significant role in the Eritrean context. Although the literature indicates that the governments of LDCs are indeed motivated to implement privatisation policies with the assistance of aid agencies such as the World Bank and IMF (Craig, 2000; Cook & Kirkpatrick, 1995), in the case of Eritrea the introduction of privatisation was initiated by the national government on an independent basis. Aid agencies did not have any influence on the country's privatisation process, neither during the process nor afterwards. Also the role of the TU was minimal, with the exception of a small conflict that took place with IMA, as described in chapter 5. The TU officials were in general not so satisfied with the privatisation process, and they pushed firms to form base unions and to respect employee benefits. The TU was of the opinion that there was a lack of labour enforcement, that the salaries were too low and the benefits too poor. Despite these views, however, its role was not relevant. So in this study we merely focussed on *State and Regulations*, *War*, and *Competition*. The critical problems encountered in this study that were associated with these external factors included the lack of access to forex services and to support institutions, the lack of skilled labour and political stability, and unfavourable government regulations. Some of these issues are consistent with those listed by UNIDO (1999).

***State and regulations*:** The success of privatisation is believed to be closely related to particular conditions, such as market competition, a market-friendly macroeconomic climate, and suitable policy frameworks (see UNDP, 1998; Chisari, 1997; Kikeri *et al.*, 1994). It is believed that these conditions have to be met in order to avoid problems such as, among other things, inconsistent policies, the lack of an adequate physical infrastructure, underdeveloped financial systems, and a lack of supporting legislation (Kennedy & Hobohm, 1999). In the case of Eritrea, policy documents indicate that the government aims at rehabilitating the light industries and building a strong export-oriented manufacturing sector to meet the local demand and to develop its export market (GOE, 2003). The GOE's trade policy claimed to promote liberal internal and external trade regimes to foster export- as well as import-based industries and services by providing financing assistance, promoting exports, and encouraging the private sector to start playing a leading role in both domestic and external markets (GOE, 1998). These were some of the tasks that the government had set out to do to create a suitable business environment for the private sector. However, our findings show a different reality. All case firms faced a number of impediments similar to those documented by UNIDO (1999).

First, the three case firms relied heavily on the import of raw materials, which means that they were dependent on the forex services provided by government banks, since no other source of foreign exchange was available. However, in 2001 the government *blocked the access to forex*, and the case firms were forced to look for alternative services on parallel markets at higher rates. These higher rates caused the firms' costs to rise by more than 33%, which disrupted the companies' planning, budgeting and business activities. Furthermore, in connection with customs duty and tax obligations, the government forced the firms to value their imports in local currency on the basis of the official rates. So because the companies had to keep their records in line with this policy, the 'cost principle' was violated and the accuracy of the information jeopardised. The costs seemed lower and profitability appeared higher than was actually the case, while on top of that the firms were exposed to higher taxes. Although the firms tried to report the difference in value resulting from the different currency rates (the official and the black market rate) as a *loss on exchange*, the tax office was not willing to treat it as an expense. In addition, new taxes were introduced, such as sur-tax, which was levied during the period 1998 – 2000, causing an undesirable rise in costs and a decline in profits, and excise tax, which had to be paid by both AW&LF and RSBSC. On the basis of the joint venture agreement, however, RSBSC had not expected this.

Second, mid 2003 the government issued a regulation concerning *import permits* that imposed upon firms the *usage of an L/C system*. This regulation caused a great deal of unnecessary bureaucracy, complicated the regular product import process, and closed the other options of acquiring forex and dealing with export partners. It also disrupted RSBSC's well-documented transparent method of importing raw materials via local import-export traders. RSBSC managed, however, to gain access to forex in 2004, with which it could order one batch of raw materials. This shows that RSBSC had in fact some power to operate outside the government's influence sphere, unlike IMA and AW&LF, which were not in that position. IMA's approach to this problems was, however, to enter the export market and sell its products and services at higher prices. It managed to attract clients who were willing to send the firm their own raw materials. Unfortunately, the regulations concerning customs duty, import permits, and L/C again undermined this way of working. For example, due to these regulations the exports services were treated as client inputs for which the firms had to pay tax. As a result, IMA lost its market. In addition, the government did not allow the firm to benefit from a fund granted by the World Bank in mid 2001, which was meant to be used for making investments to expand its activities and boost its export potential. This is a typical example of the difficulties that Eritrean firms encountered as a result of the fact that the government did not keep its promises.

Third, the regulation that banned the access to forex on parallel markets, which was introduced in 2004, aggravated the unfavourable effects on the activities and performance of the case firms. RSBSC was forced to close down its sales areas in Keren and Massawa, and finally it had to stop its operations altogether in 2005. It is argued that this regulation made it impossible for the owners to continue their business, although they did in fact have the means to do so. The firms expected the GOE to encourage investments and to reduce the outflow of forex from the country by making part of the inputs locally available. Besides government-owned banks there were no alternative institutions that could provide the firms with financial support, which illustrates that the Eritrean business environment was not a suitable one for privatised firms to operate in. Saha & Parker (2002) state that the absence of a well-developed financial market limits investment opportunities. Our findings support this claim; the Eritrean private sector clearly suffered from the lack of forex, while forex was of great importance to the firms in conducting their routine activities. Contrary to the claims of property right theorists, there were no institutions in Eritrea with the task of supporting the private sector. In general it can be concluded that the government's influence remained significant after privatisation.

Fourth, the government prohibited the advertisement of beverages and issued restrictions on product deliveries in the capital city. Also these developments severely undermined the firm's sales. The beverage delivery restrictions were introduced in 2004 and applied to the five working days of a week. RSBSC and AW&LF were allowed to conduct sales during a maximum of three hours per day. Of course this regulation disrupted the firms' distribution schedules, and in particular AW&LF suffered from its weakened position in the small local market, where the competition was harsh. So there was in fact no support whatsoever for the beverage industry; it had to find its own solutions to its problems.

Finally, RSBSC was affected by the measure of the Department of Inland Revenue (DIR) according to which it had to release client information to be used for estimating the firm's income. This measure gave rise to complaints of clients, who did not approve that their supplier (RSBSC) disclosed sensitive information without their consent. Although RSBSC tried to find a way not to co-operate, it was ultimately forced to send the DIR the information it required.

***War (political instability)*:** The 1998 – 2000 border war between Ethiopia and Eritrea caused labour shortages, uncertainty, inflation and salary rises. In addition, it frustrated investment policies. In all three firms the composition and quantity of manpower was affected. The qualified young employees were forced to join the military and were replaced by inexperienced female workers and older people, which undermined the firms' productivity and operating efficiency. It was difficult for IMA and RSBSC to appoint qualified employees, for example graduates from the technical schools. Although the female and older employees received training, they obviously lacked the skills and energy to perform the tasks optimally. Due to the labour shortages IMA was forced to reject several export orders that required a quick delivery. In addition, the overtime work organised to meet the delivery dates caused the overhead costs to rise.

All firms negotiated with the government to get their qualified employees back and have them perform part of their national service tasks at their work place. AW&LF and RSBSC managed to come to some kind of agreement with the government on this issue, but IMA was less successful. The situation forced both IMA and AW&LF to raise their employees' salaries in order to make them stay. Through these raises, however, their employees' salaries exceeded those paid in comparable competitor firms. Still, the continuous rise in the costs of living made it difficult for the workers to survive economically, which resulted in a growing dissatisfaction on their part. So many qualified employees left IMA. Although the situation was not encouraging, our findings show that the employees of all three firms were in fact disciplined, eager to learn new skills and hard-working.

In spite of all these difficulties, the firms tried to contain their costs, although there were elements they could not control, such as inflation and the costs of resources (raw materials, labour, energy, and utilities). As explained in chapter seven, the 9% annual salary increment introduced by RSBSC was meant to compensate the employees for their loss of income due to the escalation of the country's inflation levels. This escalation was a reflection of the country's macro-economic instability, and severely undermined the firms' profitability, since they were largely dependent upon imported inputs. In addition, the economic instability affected long-term planning as well as making investments. IMA and RSBSC's records show that uncertainty had led to a slight rise in the leverage ratios since 2001. As indicated by Chisari (1997), macroeconomic stability is certainly required for a successful realisation of privatisation programmes in LDCs.

***Competition*:** Privatisation increased the demand for inputs that were locally available and affected the firms' local sales activities. Formerly, IMA used to obtain some of its raw materials, such as textile garments and leather, from local sources, but now the quality was poor and the suppliers had diversified their businesses by conducting value adding activities. Moreover, because of the lack of qualified manpower IMA was forced to refuse export orders that demanded a quick delivery. In the case of RSBSC, the water supply was an issue. And for AW&LF it became increasingly difficult to acquire refillable bottles, since they were taken by the small liquor factories that did not have their own imported bottles. The literature states that a high degree of competition requires knowledge of cost issues, the use of performance measures, formal control, and improved MCS practices. IMA and AW&LF introduced effective MCS practices, mainly consisting of physical supervision and the selective use of internal reports.

However, they did not take steps to analyse this information (for example with the aid of modern tools of cost control) to achieve cost reduction and profitability improvements. This of course does not alter the fact that the firms significantly increased their investment and waste reduction activities.

With respect to the competition for output, we observed that clients of AW&LF chose those suppliers that first approached them. The fierce competition in the home market led to lower prices and firm profitability, and forced IMA and AW&LF to become price takers.

As already explained, the firms' profitability in terms of ROS, ROA, and ROE was poor, which was due to the impact of the war (e.g., labour shortages and the subsequent rise in salaries), the harsh government regulations (e.g., the abolition of forex, high taxes, the restrictions on product distribution and advertising, the strict control on import permits, etc), the fierce price competition on the home market, and the continuous rise in inflation, increasing both the manufacturing and the non-manufacturing costs as well as the power and fuel prices, as also stated in the World Bank report (2002a). Our findings clearly show the failure of the government to create a conducive and suitable market environment for privatised firms. The firms explicitly indicated that the implementation of their business and investment plans were severely undermined by the current situation. At the time that the privatisation policies were initiated the problems described above were not anticipated. They are similar to those presented by Kennedy & Hobohm (1999), who studied privately owned firms operating in other LDCs. It can therefore be concluded that political and economic stability in the country is a prerequisite for cost savings, price decline, the implementation of firms' business and investment plans, and ultimately, the success of privatisation as a whole.

8.6 Adaptation of the theoretical framework

According to the literature the governments of LDCs are motivated to carry out privatisation policies with the aid of agencies such as the World Bank and the IMF (Craig, 2000; Cook & Kirkpatrick, 1995), and Western donor countries. This study shows that the GOE committed itself to the introduction of privatisation on the basis of its expected outcomes. The GOE believed it would bring economic growth. In our theoretical chapters we discussed the arguments of privatisation proponents and their expectations with regard to the privatisation outcomes (changes in firms' MCS practices, firm activities and performance). Our observation is that the current literature does not sufficiently explain how expected post-privatisation changes take place in the context of LDCs. Former contingency-based studies have attempted to clarify the way in which some factors shape MCS practices, but they neither related these factors with the issue of privatisation nor did they place them in the context of LDCs. Recently, some studies were published that present a number of external factors drawn from the institutional theory, which shape MCS practices (Hopper *et al.*, 2004a). And although there are studies that indeed link the success of privatisation with the influence of market and country conditions, in general the research conducted in this field does not provide a detailed account of the way in which the interplay of contextual factors influences privatisation outcomes. In our study we have made an attempt to approach post-privatisation outcomes in a wider spectrum. To conduct our research we developed a theoretical framework. We argue that post-privatisation changes in the MCS practices as well in as the business activities and performance of firms are closely related to contextual factors (see figure 3.3).

To carry out our research we chose the case study approach. As explained in chapter four, the data analysis during the pilot study phase helped us in refining our theoretical framework. In addition, the pilot study enabled us to gain an initial impression of the Eritrean business environment, so we could determine practical issues and assess the relevance of the contextual factors selected. After establishing the relevant contextual factors we classified them into internal and external factors. The internal contextual factors included size, capacity to learn, technology changes, strategy changes, and the capacity to undertake action. The external factors were state and regulation, the TU, aid agencies, war, and competition. All of these factors were analysed systematically in our case firm chapters. This chapter has presented a cross-case analysis of the post-privatisation changes by focussing on the similarities and the differences of our major case-specific findings (see section 8.4). In section 8.5 we came to the conclusion that in the privatisation process of our case firms' aid agencies played no role whatsoever, which does not apply to other LDCs. In our study, privatisation was solely initiated and carried out by the GOE. Furthermore, the external factors like Culture as well as Race and Ethnicity appeared irrelevant in our study, so they were dropped. The same applied to TUs and Aid Agencies; since they did not offer data relevant enough to increase our understanding of post-privatisation changes, they were removed from the conceptual framework.

The success of privatisation depends on particular preconditions, such as the establishment of support institutions, solid policies and regulations, the provision of training, and a labour market with a sufficient number of qualified people. The literature shows that a suitable environment in which these preconditions are met (Chisari, 1997) is missing in many LDCs (Kennedy & Hobohm, 1999). It appears that the situation is not different in Eritrea. The Eritrean business firms were not offered a suitable environment to operate in, and neither did they receive sufficient support of the government. On the contrary, in addition to the inconsistent macroeconomic policies that exposed the Eritrean private sector to inflation and high costs (World Bank, 2002a), the government regulations formed the main obstacle to a favourable healthy business climate. During the period of data collection, we realised that it was useful to include the transition period into our research. In this period the government's responsibilities were determined and the sale and purchase agreements concluded. By integrating this period, we could establish whether the government had fulfilled its promises and whether the companies' performance was in line with the expectations. On the basis of the aforementioned we would like to refine our theoretical framework by specifically emphasising the role of the government. The role of the government should therefore be included as a single individual factor (see figure 8.1 below).

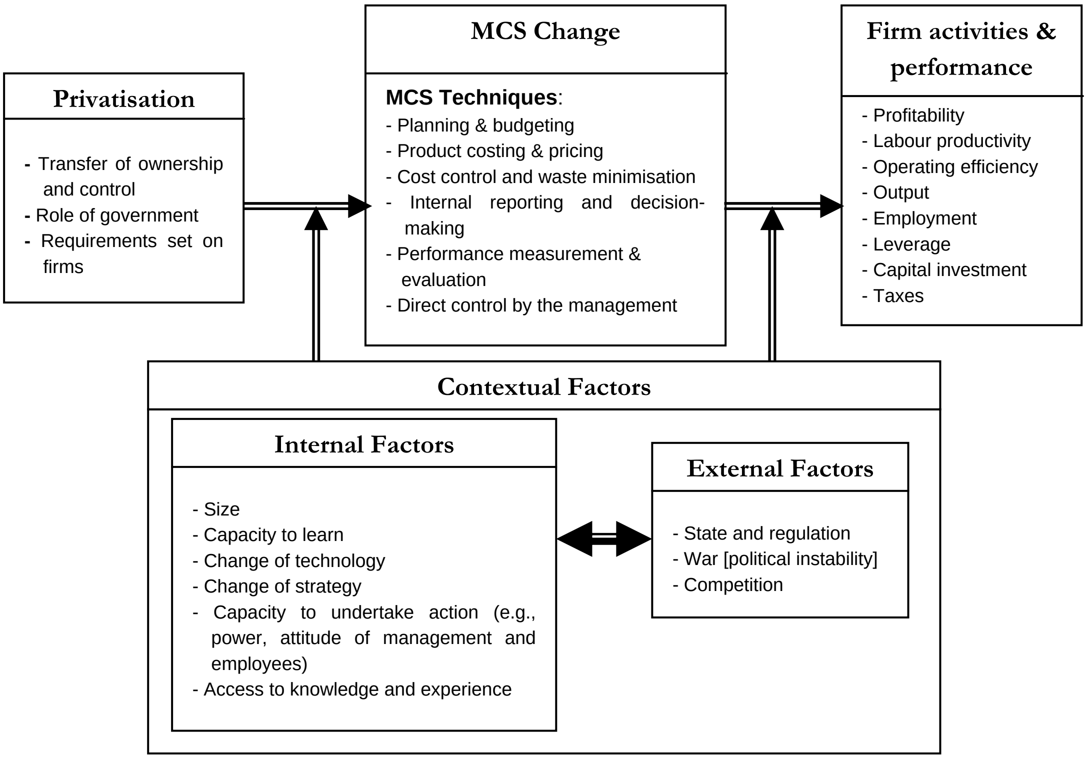

Figure 8.1 *Revised Conceptual Framework:* The relations among privatisation, MCS change, firm activities, performance, and contextual (internal and external) factors.

Furthermore, a refinement is needed of the lists of MCS techniques and the internal factors as presented in figure 8.1. Our study shows that informal controls, such as a direct supervision by managers, played a larger role in IMA and AW&LF than in RSBSC. This can be explained by the small size of these two firms and the physical presence of the owners. These informal controls replaced some of the formal tools, such as budgeting and inter-departmental reports. Therefore they should be added to the MCS techniques already listed. We also observed the involvement of family members in IMA and AW&LF. In the case of RSBSC, on the other hand, the active involvement of a multinational made a significant contribution to the realisation of MCS change by giving access to knowledge, experience, and resources already available. We found that studying both family owned firms and companies operating under the supervision of a multinational formed a good basis for comparison. Therefore we chose to add *access to knowledge and experience* to the list of contextual factors. This factor would allow us to increase our insight into the influence of multinationals on firms in LDCs.

Next, our findings show a particular degree of interaction between the internal and external factors. *First*, the government's regulations that prevented the access to forex damaged the firms' investment plans and growth strategies to achieve goals such as productivity and sales increases, market expansions, and the appointment of additional employees. *Second*, the political instability (war) diminished the availability of manpower, which limited the firms' size and their activities and caused a loss of export market. *Third*, with the help of CCC, RSBSC was able to avoid some of the government's restrictions. In spite of the unfavourable business environment in Eritrea, RSBSC managed to expand its market, to create jobs (both within and outside the firm, for example for agents), to compensate its employees for the adverse effects of inflation, and to receive support from CCC in terms of cost discounts. *Finally*, both IMA and AW&LF managed at a certain point to find their own means to obtain forex. We see that the efforts of the case firms played a role in counteracting the harmful effects of the external factors. In order to show the relation between the two contextual blocks, we added an arrow between them.

If change is viewed as the introduction and implementation of new MCS practices, the example of RSBSC shows that the influence of a multinational stimulates the attainment of the expected results. The firms owned by local people, however, did not introduce all of these newly developed MCS practices. So it appears that multinational firms have a greater capacity to undertake action. Another important determinant was the interest and background of the owners, either to facilitate MCS change or to hinder its development. Further, we observed that the introduction of modern MCS practices (e.g. the total quality system, the detailed operational control system used by RSBSC) caused no problems. This finding rebuts the claim that Western MCS techniques are not suitable for LDC firms. However, more research is still required to come to a definitive statement about this matter.

In general, the outcome of privatisation with respect to our case firms can be summarised as follows. Privatisation intensified investments, and it improved the firms' productivity, product quality, operating efficiency and output. Further, it resulted in a significant reduction in waste, it changed the mentality of both the employees and the owners, who became much more involved. In addition, the leverage ratios of all three firms declined. This shows that the firms no longer relied on bank overdraft to finance their activities. See for further details the comparative firm performance discussions in section 8.4. On the other hand, in the cases of IMA and AW&LF, firm performance and MCS improvement was hindered by the lack of experience of the managers and/or owners, which corresponds to findings of case studies conducted in Bangladesh and Sri Lanka (Hopper *et al.*, 2004a). Also these findings were obtained by including socio-economic and political contextual factors. So in order to make a reliable analysis of post-privatisation outcomes we strongly support this approach. Our theoretical framework was broad enough for addressing post-privatisation changes in a wider scope. We have studied MCS practices and firm performance during both the pre- and the post-privatisation period. In this way we could determine the changes that took place in the firms. So the inclusion of both the pre- and post-privatisation periods and the contextual factors has made our framework a comprehensive and helpful tool for studying our research topic in its broader context. In the case of LDCs this is particularly important since the business environment and conditions there are often not favourable. We hope that the empirical evidence gathered in this study has increased the general insights into the developments in the MCS practices, the firm performance and firm activities of LDC firms (see for more details section 8.5).

The contextual factors drawn from the contingency theory and the institutional theory were useful since they allowed us to make a thorough analysis of the post-privatisation changes in MCS practices, firm performance and firm activities. We believe that the theoretical framework can be suitably adapted to similar situations in other LDCs. However, there are some specific issues that need attention, such as the nature of the government's interaction and regulations, the degree of competitiveness of the market, culture, the level of economic growth, the institutional environment, the type of firm ownership, and firms' managerial capacity. If these issues are properly addressed and if the relevant internal and external contextual factors are taken into account, similar studies could be conducted with this model. We believe that our research has made a contribution to the development of a structure that enables researchers to study MCS practices and firm performance from the perspective of LDCs.

8.7 Implications for actual practice

8.7.1 Implications for the case firms:

We recommend the following steps for improvement. *First*, the production capacity of IMA and AW&LF is relatively large in comparison with their local competitors. This indicates that both firms could maximise their productivity to such a degree that they could gain advantage of economies of scale, since unit costs decline as the production volume increases. This would enable them to sell their products at lower prices than their competitors. During the time of study, both firms' competitors were setting lower prices, making IMA and AW&LF price takers. But assuming that these competitors spent the same amount of input costs while their capacity was lower, one would not expect them to set these low prices. This issue demands further investigation. An explanation could be that both firms had problems with their costing systems. IMA and AW&LF should make a critical assessment of their cost accumulation and allocation methods in terms of cost reduction. In addition, as both firms are focussed on low price strategies, it is advisable to aim at realising cost efficiency (see Chenhall & Langfield-Smith, 1998b). Both firms could consider using the available MCS tools to look for possibilities to reduce costs, so they can offer lower prices. Our findings indicate that the quality level of both firms' products was relatively better than that of their competitors. The customers, however, preferred the cheaper products, even though they were of lesser quality. And since our case firms are not willing to compromise their quality strategies, it is important that they either revise these strategies or increase their efforts to convince the customers of the advantages of a product of good quality.

Second, IMA and AW&LF need to improve the accuracy of their costing systems as well as the timing of their reports. In this respect, additional investments in the computerisation of their information systems would be beneficial, which would also facilitate the introduction of improved MCS. Further, IMA may consider setting up a Marketing Section, and AW&LF should strengthen its Marketing Department. A marketing unit provides information on the way in which competitors operate in the home market. And as RSBSC has shown, non-financial information is useful in developing strategies to attract more customers and to survive the competition. *Third*, IMA and AW&LF need to introduce an incentive system to motivate their employees by sharing profits. If the workforce is sufficiently motivated and content, firm performance will increase. *Finally*, both IMA's and AW&LF's managerial and accounting staff is too limited in size and insufficiently qualified. We suggest that both firms need to upgrade their managerial capacity in order to enhance the utilisation of accounting information. Moreover, the sophistication of MCS practices should go hand in hand with improving the knowledge and skills of the accounting personnel (see Ramaswamy, 2001; Ramaswamy & Von Gilnow, 2000; Shirley & Nellis, 1991). These issues can only be improved, however, if simultaneously the unfavourable government regulations and unstable political climate are dealt with.

8.7.2 Implications for the government bodies and aid agencies:

Normally, government bodies are expected to facilitate the process of privatisation by creating a conducive business environment consisting of financial markets and private banks. In addition, the government should ensure the supply of trained manpower as well as stable macro-economic policies and regulations. Further, it should encourage firms to enhance their export activities. Our findings, however, show that the case firms encountered many challenges. As already indicated, the government regulations concerning the forex services and import permits greatly affected the activities of the case firms. In addition, the tax levels were high in proportion to the revenues, while a number of new taxes were introduced during the post-privatisation period. Other restrictions of the government included an L/C system as the sole option for import-export activities, the time limits on the distribution of beverages in the capital city and the prohibition of advertising beverages. These measures disrupted the firms' operations severely, and even led to their termination in some cases. Although privatisation was supposed to recover firms' autonomy, during our research they were experiencing extreme pressure as a result of the governmental policies.

Our findings support the statement of De Haan and Simermann (1996) that economic performance depends on political and institutional factors. We would like to bring the following to the attention of the relevant government bodies. The primary role of the government is to create a favourable business environment. This is imperative. The government is expected to provide skilled labour and financing facilities. It should adopt stable policies and fulfil its promises. It could also encourage investments to diminish the import of input to minimise the flow of forex. So a conducive business environment without any interference is deemed to be vital to the realisation of a successful private sector (Kennedy & Hobohm, 1999). Our findings show that the interference of the Eritrean government had huge consequences for the outcome of privatisation. As we can see the situation became quite severe for our case firms. Our result also indicate that the involvement of a multinational (as in the case of RSBSC) proved to be highly beneficial in terms of financing as well as sharing the knowledge and experience essential in conducting business in a successful manner.

In this respect, we expect of aid agencies, such as the World Bank, that they let themselves be informed properly about the situation in the county in question. Further, they should encourage the government to play a positive role in making privatisation a success. In addition, aid agencies could support governments in creating a favourable business environment. Our case firms indicated that they wanted to continue making investments, but that they needed access to forex. Supporting firms in making investments will stimulate employment as well as the increase in firm size and activities. We believe that the success of privatisation serves the interests of the government, investors, and society as a whole. Moreover, if governments actively support and facilitate privatisation, the provision of huge resources by aid agencies afterwards will not be necessary. It is therefore of the utmost importance that aid agencies and development partners convince the governments of developing countries to do everything they can to facilitate the establishment of a strong private sector.

8.8 Limitations of the study

During the course of this study we discovered that it was difficult to get access to data. The owners and managers of the firms did not seem to recognise the benefits to be gained from our research output, and were therefore reluctant to disclose their data. As a result, the number of firms we studied remained limited. So firm owners and managers could be made aware of the advantages of the participation in research studies by the provision of information and training. This training could also be directed at the type of data suitable for sharing with scholars. In addition, the data bank of the Ministry of Trade and Industry is incomplete. Another problem was the difficulty of obtaining data from the pre-privatisation period as well as finding respondents who could give information on the MCS practices in the public ownership period. For example, in the case of AW&LF, we did not manage to find accounting staff members who had also worked with the firm during the public ownership period. Moreover, our case firms had not kept their pre-privatisation financial records, and the information that the MTI could provide was incomplete. In some cases, this complicated the assessment of issues such as leverage, past employment trends, capital investment and taxes.

Next, we want to raise an issue with respect to the interpretation of the study's results. The privatisation process in Eritrea was undermined by the border war with the neighbouring country Ethiopia. As explained in detail, this war had a tremendous impact in terms of labour shortages, the drainage of hard currency as well as a significant rise in inflation and the costs of living. It is highly likely that the outcome of this study had been different if the situation in the country had been peaceful at the time of research. If the war had not started, the firms would have had sufficient manpower and a better access to forex. In addition, they would not have had to suffer as much from the government regulations, which mainly resulted from the situation after the border conflict. As we observed that the firms were highly motivated to implement their business and investment plans, it is very probable that, had the situation been peaceful, they would have succeeded in expanding their markets, increasing employment, and enhancing their production, sales, and profitability. Further, to obtain a broader picture of the impact of privatisation it is advisable to extend the post-privatisation period. Of course in our case this was not possible, since the timing of our study did not allow us to do so. The most recent financial audits we collected dated from 2003. We therefore point out that the findings of this study should be interpreted with caution and not be associated with the results of privatisation studies conducted in other LDCs, where there is peace and stability.

There is little literature that explains MCS practices form the perspective of firms in LDCs. Neither is there much literature available about the impact of MCS change on firm performance in the context of LDCs. Research dealing with this topic includes studies conducted in Bangladesh and Sri Lanka. The scope of these studies, however, is much more limited. We tried to compare our findings with those of former studies in section 8.4., but found that as yet no similar studies have been carried out in Eritrean firms. In order to describe some concepts in chapter three and to review some relevant empirical evidence, we therefore had to turn to Western-based literature conducted in this field. The former studies on MCS change addressed in chapter three are mostly surveys, which merely give an account of the implementation of new MCS practices in privately owned LDC firms. Most of the studies that analyse MCS practice change have been conducted in the West. The majority of these studies do not pay much particular attention to the way in which the same techniques are used after a change in ownership. We therefore had no significant empirical evidence to compare our findings with.
This study attempts to make a link between the influence of contextual factors and MCS practice changes, firm activities, and firm performance. It has become evident that this relationship is complex, and we realise that this research field still requires a great deal of exploration. Therefore more empirical findings have to be gathered by similar case studies.

8.9 Suggestions for further research

It is apparent that the body of literature still lacks sufficient knowledge of MCS change, firm activities, and firm performance in privatised LDC firms. We therefore encourage accounting researchers to conduct more case studies on privatisation in LDCs. Particularly cross-country comparative case studies will provide more knowledge about the effects of privatisation and the influence of contextual factors. In this respect, we are convinced that our basic conceptual framework could serve as a stepping stone for similar future studies. As we indicated in section 8.6, some modifications might be required in selecting the relevant conceptual factors, the range of MCS techniques to be investigated, or the tools to be used for measuring firm performance. Furthermore, we suggest that researchers may consider conducting comparative case studies that focus on identical firms in similar industries in similar periods for each country. In this way, the MCS practices and firm performance of privatised firms could be compared to that of firms newly started as private entities. A further focus on the post-privatisation period would diminish the need for data from the public ownership era, and would make the search for respondents that could provide data on past MCS practices no longer necessary.

So a wider time range and the incorporation of contextual factors are two important issues in future research. In addition, before finalising one's research design and starting the actual study, it may be advisable to first conduct a pilot study. This procedure proved to be very helpful in choosing the relevant elements for the framework, and it guaranteed a solid basis for the study. We believe that a solid basis makes the research and its outcomes more reliable.

We have seen that it is difficult to explain the changes that have taken place solely on the basis of the introduction of privatisation or the adoption of new or improved MCS practices. For example, attracting foreign customers who do appreciate quality is possible by making firms committed to their quality strategies and via introducing strict quality controls. In addition, employees can be trained in internalising quality in their mentality and way of working. Other issues, however, such as profitability increase, operating efficiency and employment, are related to other factors. A broader sample of firms would shed more light on the relationship between the contextual factors and the firm performance results.

Finally, we argue that future researchers should clearly define their domain within the range of studies emerging in this field. This also involves choosing the proper methodology. In addition, in order to increase the validity and reliability of the conclusions as well as the robustness of the results, a larger number of firms in more sectors should be studied. This expansion of the research area would pave the way for comparative analyses among studies conducted in different places. These analyses and follow-up studies might then be structured on the basis of surveys administered across a large number of countries. And in this way a solid basis would be created, enabling researchers to start making reliable generalisations.