

"National Policy-Makers' Experience: New Zealand"

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Thank you for the opportunity to talk about New Zealand's experience in corporatising and privatising state business enterprises, in order to improve the contribution they make to the well-being of New Zealanders.

It is clear that privatisation can serve a variety of different purposes. Some are complementary; others conflict with each other. The objectives, explicit or implicit, of governments engaged in privatisation programmes around the world have, for example, included improved economic performance; improved management and control; improved consumer choice; more flexible labour markets; improved productivity; generating more revenue for government; reducing government debt; promoting popular capitalism; and promoting employee shareholding.

You get a much better price if you privatise a protected monopoly, provide a tax holiday to get it off to a good start, and guarantee government purchases of the output at favourable prices. On the other hand, that approach produces nothing whatsoever by way of efficiency benefits. On the contrary, it can lock existing avoidable costs into the economy as a whole.

The objective of reform in New Zealand has, at every stage, been to maximise net benefit to the consuming public. It has been our aim to obtain the highest sale price achievable--but subject always to that objective. Deregulation and the encouragement of competition have been seen throughout as fundamental to the public good. We have sacrificed sales revenue without question where necessary, rather than privatise a monopoly.

State businesses in New Zealand have been going through a two-stage reform process since 1985. Most state businesses have been converted from their original departmental structure into state-owned limited-liability companies or corporations, in the first instance. Subsequently, once the business has improved its performance, and after the government has tidied up the regulatory environment, reform moves on to the second stage of full privatisation.

This mode of development has not occurred as a result of any particular philosophical position adopted a priori by the Government. Traditionally, the New Zealand Labour Party has, for 50 years, been opposed on general philosophical grounds to most of the reforms implemented by the present Labour Government since it took office in 1984.

We had a situation in New Zealand where the attitudes, policies and philosophies adopted by both our major parties for 30-50 years have been seriously out of touch with reality--and a liability to the nation.

From the early 1980s onwards, however, a rapid evolution occurred in the thinking of the present Labour Cabinet and Caucus, as a practical response to the profound economic and social problems that had emerged over time as an outcome of our traditional approaches to policy.

Back in the early 1950s, New Zealand used to have a dynamic, innovative land-based economy that was earning us the 3rd highest living standard in the world. But ever since

the 1930s depression, we had been steadily raising barriers against international competition.

The goals of protectionist policy were increased urban employment, and increased protection against international economic shocks. But it also caused our manufacturing to develop high cost structures that, in large degree, precluded those industries from exporting. Over time, the costs thus imposed on the economy gradually reduced the competitiveness of our agricultural exporters.

These problems were further intensified by Britain's entry into the EEC, and by the oil shocks of the 1970s. Balance of payments problems became endemic.

The then Government, instead of facing up to the real problems sought to compensate farmers for those costs by subsidising them to boost export production. Public money was also used to persuade uncompetitive manufacturers to enter the export business and improve our foreign exchange earnings.

With the same objective, the Government underwrote multi-billion dollar energy projects that had been rejected by the private sector as a bad commercial risk. Returns proved to be zero or negative.

In 1982, as the imbalances worsened, prices, wages, interest rates and rents were all subjected to direct controls by a conservative government. The distortions in resource allocation that were the underlying cause of our problems were compounded.

Our inflation, in the 10 years to 1984, was 1½ times the OECD average; our economic growth rate was half the OECD average; net public debt multiplied six times over; and debt servicing mushroomed from 6.5% to 19.5% of total government spending. Unemployment rose from 5000 to 132,000 with no sign of stopping.

The damage done by excessive protection is even clearer if a longer perspective is taken. In the 25 years to 1984, our average annual increase in productivity was, at 1.2%, the lowest in the OECD. Japan averaged 5.8% and the EEC 3.3%. By the early 1980s, our living standard was thirty-second in the world - not third. It had been falling by an average of one place a year for 30 years.

When do you call a halt and think again?

On the other hand, it would also be fair to say that, for a generation, most New Zealanders had seen high protection, not as a problem, but as the main safeguard of both employment and prosperity. Whenever problems arose, the normal government response in New Zealand was to lift protection a notch or two higher, to comfort those most affected.

By 1984, that whole approach was no longer sustainable. A run on the dollar occurred during the 1984 election campaign. By the time we took over, the banks had been forced to close their doors to all foreign exchange transactions. This was, then, in brief, the broad economic environment within which state sector business activity had been evolving for 30 years or so.

State-owned businesses in 1984 accounted for 12½% of GDP and 20% of total investment. (Our whole agricultural sector amounts to only 8% of GDP.) Those businesses included, for example:

- The country's largest trading bank, plus the bank responsible for a lion's share of lending to the agricultural sector:

- The industries responsible for generating and distributing wholesale electricity:
- Most of the coal industry; 50% of our plantation forests; all railways and telecommunications:
- A lot of the radio, all the TV; a tourist hotel chain; an internal airline monopoly:
- The post office; huge interests in the construction of major state projects:
- A film production company; a printing company that did all government's printing work:
- Land development activities; a petroleum corporation - and so on.

The largest of them - the post office, which included post, a retail bank and the telecommunications monopoly - was twice the size of our biggest private sector corporation.

It had been calculated that a 1% rise in the rate of return they achieved would be enough to increase the GDP of the nation by 0.6%.

On the other hand, like the rest of the New Zealand economy, they reflected the ruling philosophy that both parties had shared for something like 50 years. They were highly protected non-profit-making state-owned monopolies in most cases.

Among the general public, that was, on the whole, perceived to be a good thing - not a bad thing. People felt they saved substantially on power, coal, telephones and so on, because their bills did not have to include any component either to cover profit; or to provide for the advertising costs that are inevitably involved in competitive private sector business.

Nobody thought that government services were very efficient, but on the whole, they were seen as a pretty good deal. The relationship between these inefficiencies, the performance of the economy as a whole, and the living standard of the community was not widely perceived.

The 1984 election proved to be a watershed in New Zealand history. Within 3 years from that date, New Zealand went from being one of the most highly regulated economies in the OECD to being one of the least regulated.

We freed interest rates, introduced a firm, anti-inflationary monetary policy, removed exchange controls and floated the New Zealand dollar. We phased out import licensing, and reduced tariffs across the board. Virtually all subsidies, tax perks and lending concessions for farmers were phased out.

The finance industry became one of the most deregulated anywhere in the world. The labour market, though still by no means the most flexible in the world, was made more responsive to market opportunity.

We reduced the top rate of personal income tax from 66% to 33%, and company tax from 45% to 33%. A wholesale sales tax with rates from 0-60% was replaced by a flat-rate 10% consumption tax across virtually all goods and services without exception.

The thrust of our policies was to put producers back in direct touch with their markets; to make them dependent on returns from the market; to expose all sectors, but particularly sheltered sectors, to increased competition; to level the playing field so that resource would flow automatically into the areas giving the best returns; to improve the incentives to effort

and innovation; and thus encourage markedly better use by players right across the board of the resources they were consuming.

The reform of state owned business enterprises was therefore just one thread in a very much wider pattern of structural reform. To have a positive value to society, the output of such enterprises needs to be worth at least as much as the resources used to produce it. Their outputs need to be supplied with the least possible consumption of resources.

Neither of those criteria, however, had ever been central to the concerns of government or the managers of state businesses. They were controlled in the traditional departmental way by rationing inputs such as budget and staff numbers. Outputs, efficiency and performance were taken for granted or ignored.

Over the years, state owned enterprises - now known as SOES in our local jargon - had been given a conflicting mix of business, social and regulatory responsibilities. But neither ministers nor managers had any idea how much priority they were supposed to place on business efficiency, or how far they should forget it, in order to create jobs, provide cheap goods to the needy, or meet other social priorities.

Ministers, who were certainly not experts on business, ended up making business decisions. Commercial managers, right outside their own field of expertise, were forced to make social decisions. The outcome was reported to Parliament, but nobody knew what it meant. Responsibility was so blurred and divided that nobody's neck was ever on the block over the results.

Conflict between commercial and regulatory roles introduced unfathomable complexities. State Coal, for example, owned a majority of our coal mines. As regulatory authority for all coal mining, it had to decide whether new licences should go to its own commercial operation - or to private sector competitors!

Thirdly, SOEs often got their capital free from the government. They did not pay tax or dividends. This and many other factors created a situation where the costs appearing on their books bore no real relationship to the true cost of their activity. No one can manage that kind of system efficiently. The system does not produce the basic information required to do so.

A massive review of SOES was therefore initiated, focusing on basic structures, and business systems. We knew the results would be bad, but none of us had the remotest idea how bad they really were, until the detailed results began to pour in.

The state coal industry, for example, was managed entirely on a cash-in, cash-out basis. It had lost money for 20 of the previous 22 years, but with government picking up the tab, state coal was capable of setting prices that made life close to impossible for private competitors, without risk to itself.

The Post Office Savings Bank had lost half its market share in 10 years, but in that same period, its spending had risen by 75% in real terms. The organisation managing government property was paying bills on property it could not even identify. The only single-story building in the main street of Wellington was owned by the government. Its existence had been ignored ever since 1926. In downtown Auckland and Wellington, we were earning a zero return on four prime sites worth \$50 million.

Losses on the postal service were forecast to reach \$1 million **per week** by the following year. Inventory practices were, in general, a nightmare. The value of Post Office stocks had risen from \$186 million to \$403 million in 18 months. Equipment was becoming obsolete in

their stores before they were able to install it. They had 2 years' supply of dial telephones when hardly a customer in the country wanted dial telephones any more.

Sloppy coordination was the norm. The Electricity Department had built a major power station on top of one of Mines Department's best coal seams. A new staff hostel actually subsided before it could be occupied, because the other department was mining coal underneath it.

The Post Office managers in charge of postal services, banking and telecommunications categorically stated that they could not be held responsible for the financial performance of their businesses - they did not have control over any of the functions fundamental to business success. In other words, financial performance was a sort of residue. It was anything you had left over, after the Ministers and control departments had finished with your outfit.

During the previous 20 years, the government had poured \$5 billion of the taxpayer's money into these areas of activity. The return on that investment in the 1986-87 year was zero.

I therefore set myself to develop new principles designed to shift SOEs on to a commercial basis. The State Services Commission thought the idea much too radical. The Audit Office took umbrage - it infringed their authority. Some of the trading departments dug in for a long defensive war.

The progress of reform bogged down. Every conceivable attempt was made to delay, sidetrack, relitigate and reinterpret the thrust of the principles, and turn the government's nose in some other direction.

In the end, the log-jam was broken when, in December 1985, I announced a new set of principles for SOEs:

- State trading activities should have purely commercial objectives. If the government requires any non-commercial activity to be carried out, that work should be budgeted clearly as a separate government activity. It would not be buried any longer within the trading activity of the state owned enterprise.
- SOES should operate in a competitively neutral environment without advantage or disadvantage over other players. They should be set up with a normal commercial balance sheet. They should fund their activity in the normal way from the market, without concessions or guarantees. They should pay tax and earn a normal commercial return on the risk capital invested in them; operate under the same safety, labour market and environment rules, and so on.
- They should be organised in a form designed to facilitate the implementation of those principles.

Henceforth, directors and managers would be given clear business goals. They would have the autonomy to make their own decisions about how to achieve those objectives; the owners would hold them accountable on the basis of their performance in doing so.

A State Owned Enterprises Act introduced in 1986 created nine new SOES to take over the trading functions previously handled by government departments: Airways, Coal, Electricity, Government Property, Land, Forestry, NZ Post, Post Bank and Telecom Corporation.

They were established under the Companies Act as autonomous limited liability companies with full legal power and appropriate accountability to both lenders and owners.

That set in motion an enormous process of change affecting one-eighth of the total economy.

Among the most important lessons learned from all our experience, let me emphasise this one as central - quality outcomes start with quality people. Getting the policies right will not be enough unless you also get quality people into all the strategic positions at the right time.

The State Services Commission, for example, had a central role in the transition process. It was headed by a bureaucrat of the old school. He did not believe that state enterprises should be commercial. His replacement, Dr Roderick Deane, formerly deputy governor of the Reserve Bank, played a crucial role in helping us to achieve rapid change. Dr Deane had the drive, will and capacity to make things happen.

Equally important was the calibre of the boards of directors appointed to the new organisations. Tokenism and party track record were ruled out from the start as irrelevant to the selection.

We wanted the best possible people from the highest levels of private sector management. The switch to a commercial approach created enthusiasm throughout the business community. In that climate, we were able successfully to recruit some of the country's most dynamic and experienced business people as directors. Informed sources have commented since that making Sir Ronald Trotter chairman of Telecom -and the board's subsequent appointment of Dr Peter Troughton as CEO - may well increase GDP by up to 1%, compared with the likely outcome for the nation with Telecom under its previous management.

Men like Alan Gibbs, Chairman of New Zealand Forest Corporation, have understood the benefits to the nation of the competitive principles underlying the changes. So he had no hesitation in pressing forward on a fully competitive commercial basis. In one or two other cases, however, certain new boards have allowed themselves to be tempted by monopoly rather than competitive responses to the challenges facing them.

Where the government permits that, directors can look good without bothering to achieve the real economic objectives.

At the heart of these changes, there was a complete alteration in the way we had traditionally conceived of the role of Ministers in the system.

Theoretically, Ministers had always known everything, decided everything, and were responsible for everything. One of my first jobs as Finance Minister in 1984 was to authorise an expenses payment of \$400 to an air force officer who had been stationed for a time in Fiji. I had no way on earth of knowing whether they were justified or otherwise. That was what we used to call accountability. The system was preposterous.

At an earlier stage during the 1970s, I had been Postmaster General. I thought I was running the Post Office with its 30-40,000 staff - one of the nation's biggest businesses. But a Minister is in Cabinet on Mondays; involved in Cabinet committees on Tuesdays and Wednesdays; in Caucus on Thursdays, and in Parliament 3 nights a week until 10.30 pm. No chief executive on earth can manage a business that way.

What Ministers had actually been doing was signing off pieces of paper brought to them by the organisation.

Under the new system, once you have appointed a strong board and managers, the minister is free to focus where he should - on overall objectives, goals, strategy and priorities.

His most important single responsibility becomes the task of agreeing the right mission statement for the organisation; agreeing the programme on a one-to-five year basis; and monitoring performance against those criteria.

The gains from corporatisation are enormous - far greater than most people can imagine at the outset of the programme.

Our postal system lost \$38 million in 1986-87 and was set to lose \$50 million the following year. Instead it was corporatised. It held the price of basic mail, and instead of a \$50 million loss, it made a large profit.

Our Forest Corporation, responsible for 550,000 hectares of plantation forest, transformed a \$70 million loss into a \$53 million profit in one year on a turnover of less than \$300 million, after corporatisation. Its salaried staff was reduced by more than two-thirds. Its profit in the current year is likely to be around \$150 million.

Electricorp has reduced the real unit costs of electricity by 20% in two years, and will improve significantly on that in the current year. Railways reduced its staff from 21,000 to 11,000 in four years. It is still handling virtually the same number of tonnes/kilometres. Rail freight rates are down about 45% in real terms since 1983 -an enormous contribution to the well-being of regional industries.

The Post Office, the electricity, coal and forestry industries had been billing both taxpayers and consumers for thousands of workers who had never been needed at all. Not one cent's worth of benefit was given to the public in return for the payment.

Telecom has cut staff from 25,000 to 19,000 and numbers will fall to around 14,000 by the end of this year.

After corporatisation, the state coal industry found that literally half of its total staff could be made redundant without loss of output. It had been costing \$122,000 a year to keep those people in jobs. They added nothing to output. Their sole contribution was to raise costs. At one major mine, one-third of the previous workforce now produce 20% more coal.

These gains in productivity and efficiency create new benefits for every business and household across the economy. In exactly the same way, gains from micro-economic reform elsewhere in the economy are reflected back into the SOE area.

In New Zealand, port reform, transport reform, and the efficiency gains made by Electricorp have already, for example, added about 20% to the value of our forests.

It took the best part of 3 years after 1984 for all the debt accumulated by the previous administration to come out of the woodwork into the plain light of day. In December 1987, with public debt standing at around 75% of GDP, the Government announced its intention to repay on third of it - about \$14 billion - by 1992, and to do so, in significant part, via a programme of asset sales. Since then, assets sold by the New Zealand Government include:

Air New Zealand, Petroleum Corporation of New Zealand, Postbank, the Rural Bank, the New Zealand Shipping Corporation, the Health Computing Service, the National Film Unit, Development Finance Corporation, and Communicate New Zealand. The DFC subsequently went into statutory receivership.

The Government's shareholding in the Bank of New Zealand was offered for sale last year. However, the move proved controversial within the Labour Party, and the Government decided that none of the tenders was good enough to accept. The BNZ, a few months afterwards, greatly increased its estimates of losses made on bad debts.

Major assets placed on sale more recently include 550,000 hectares of state-owned plantation forest, and Telecom Corporation of New Zealand. The sale of New Zealand Railways begins to look increasingly likely. Coalcorp's sale is held up meantime pending clarification of Maori land claims. Decisions about selling Electricorp assets will not be taken until further work is completed on the regulatory environment.

The repayment of debt is obviously important, particularly for a country as deeply indebted as New Zealand. The sale of Telecom has the potential to reduce the debt burden by as much as \$3 billion. Without it, the Government could not meet its latest target of reducing debt below 50% of GDP by the end of 1992.

Net debt servicing is still consuming \$16 in every \$100 of total government expenditure. The Labour Party, though traditionally against asset sales, recognises that this limits the Government's ability to budget flexibly for desirable social goals, and places social services at avoidable risk in the case of any substantial economic shocks.

The cost of servicing the \$3 billion involved in Telecom is about \$420 million a year, every year. The reduction in annual cost as a result of the sale will be roughly a quarter of a million dollars net, allowing for dividends of around \$180 million a year.

On the other hand, debt is only one aspect of the matter, and many analysts would argue that it is by no means the most important one. I certainly agree with that sentiment.

We went to great lengths, when we corporatised state businesses, to develop sophisticated monitoring procedures to keep track of their performance. We did everything possible to insist that the new state corporations were no longer financially guaranteed by the government. We said very clearly that we would sack inadequate directors or managers, and if necessary, let corporations go broke exactly as they would in the private sector if they did not perform adequately.

Nonetheless as long as they are owned by the state, it remains difficult to make those statements fully credible in the marketplace.

Moreover, at the end of the day, nothing one can put in place for a state owned entity could ever exert as much discipline as the threat of take-over. The best bureaucratic monitoring system does not do that job as well as monitoring by professional analysts and the sharemarket.

Finally, as long as ministers are the shareholders, then no one can rule out a risk that over time, politics will exert an increasing pressure on SOE decisions, and ultimately undermine the efficiencies we had gained.

These have all been factors in our advance on a pragmatic basis from corporatisation to privatisation.

Our thinking has also been influenced by the fact that, in one sense, ownership is not the real issue - and too much of a focus on ownership can confuse rather than clarify your thinking.

In New Zealand, it was the evolution of events surrounding Air New Zealand that first focused the attention of the general public on what matters to consumers.

Air New Zealand, as a state owned business, had always done a first-class job for customers on international routes. They had to, they were competing Pan Am, Qantas, British Airways and the best in the world. But at home in New Zealand, where they had a domestic monopoly, it was a different story.

Passengers all trudged through the rain from the terminal to their aircraft. They waited up to 20-30 minutes at the other end for their luggage. Nobody realised what we had been missing until the present Government decided to break Air New Zealand's monopoly by letting Ansett come in alongside them.

Suddenly, overnight, to the utter amazement of the New Zealand public, we found that we too could have covered access to planes, just like the rest of the world. The capital city had been using a grotty old prefabricated building as a terminal ever since World War II, and nobody had been able to get it upgraded. Suddenly we had two totally modern terminal buildings. We got more flights, cheaper flights, better food, friendlier service and virtually a zero wait for luggage.

People began to see, often for the first time, that the central issue in safeguarding their own interests as consumers was not, in fact ownership, it was competition. We were getting increased efficiencies because we were exposing state monopolies to competition or the threat of it. We had given them a form of management that allowed them to respond constructively to that threat. The outcome demonstrated that competition is far more effective than either ownership or regulation in extracting efficiency from business operations on behalf of the owner, and performance from it on behalf of the consumer.

The Air New Zealand case illustrates very clearly that a Government has to be clear about its objectives from the outset.

Air New Zealand was on our list of businesses to be sold. Letting Ansett in as a competitor clearly reduced the value of Air New Zealand to the Government as a shareholder. But you have to ask yourself: What are we trying to accomplish? Are we aiming primarily to improve the value of Air New Zealand? Or is our main aim to give passengers and shippers of air freight a better deal that improves economic activity?

Competition is what drives the innovation required to find continuously new and better ways of doing things in business.

On the other hand, wherever there is competition, there has to be risk. Questions then arise about who should be taking that risk. Should governments force their taxpayers into the front line in major battles between rival commercial airlines or telecommunications suppliers?

A growing number of people today say the government does not need to do that to achieve what it wants, on behalf of the nation.

The evolution of thinking in New Zealand is illustrated in every respect if we look at Telecom Corporation.

Telecommunications became a state monopoly more or less by chance, on the whim of a single individual, in 1881 - about the time when the first telephone was landed in the country.

Telecommunications have been run, along with two other totally unrelated businesses - a retail bank and the postal service- by the Post Office Department. By the mid-1980s, virtually every household and business in the country was linked into the system. New Zealand business spent about \$767 million on network services in the 1986-87 year.

But "universal service" was not quite the way most customers saw what they were getting from the old system by the mid-1980s. Service? According to customers looking back now at that period, there wasn't any. The customer was not a major consideration. The Post Office didn't bother to offer options. It had no incentive to investigate the latest overseas technology.

For hours at a time, it was sometimes impossible get call through from Wellington to Auckland. Faults took as much as six weeks to fix, but when the truck arrived, it always brought three technicians to do one man's work. Toll charges were several times higher than anybody could ever justify, based on what they actually cost.

Internally, the mess was even worse than it looked from the outside. It was post office policy to pay cash before goods were received. Our review found 13,000 faulty telephones in stock, from one overseas manufacturer, and \$30 million worth of PABX gear was sitting in store, waiting for someone to remedy defects in its software.

Looking at that mess, the government decided that corporatisation alone could never solve all the problems. We decided to open the market to competition.

We looked at all the options. We wanted to avoid an onerous regulatory regime that might stifle innovation or deter entry. We were not impressed by the Oftel approach of the UK. The alternative was to rely on our Commerce Act, the general legislation we use to promote competition. The general law is neutral as between competitors. The ground rules are already clearly set and widely understood.

Regulatory authorities tend, sooner or later, to be captured by vested interests. Some countries that have set out to deregulate telecommunications ended up finally with more regulation than they had when they started. Excessive regulation slows down the pace of change, often unnecessarily. Those delays are costly for the firms involved. One independent report estimated that if the average delay in installing leased lines to new buildings could be shortened from 6 months to 2 months, then our GDP would rise by \$85 million a year.

The Government therefore opted for something not so far adopted anywhere else in the world, the complete deregulation of the telecommunications industry.

Telecom's statutory monopoly was removed under the Telecommunications Act 1987. There are no specific regulations or regulatory body for the industry. Market players including Telecom are subject to the Commerce Act and scrutiny by the Commerce Commission. Operators of overseas services have to be registered. They are subject to uniform terms and conditions when dealing with overseas carriers.

Telecom's special rights of access to land have been curtailed. No restrictions have been placed on foreign ownership of competing services other than the provisions of the Overseas Investment Act. Any other government agencies wishing to enter the telecommunications market must do so on a fully costed and commercial basis.

It is an ironic situation. In 1881, New Zealand was one of the first countries to form a state monopoly for telephone services. In 1989, we became one of the first nations to fully deregulate its telecommunications industry.

The response of the corporation to deregulation has been dynamic.

The company is investing about \$600 million a year in new technology. Staff numbers have been reduced from 25,500 to 17,500 in 2½ years and will fall further to about 13,800 in the next 2 years. Productivity has improved dramatically. In 9 months, the number of circuit ends per staff member increased from 81.27 to 99.48-more than British Telecom was able to achieve in 3 years.

Eighteen months ago, digital lines served only 35% of Telecom customers. That is now 70% already, and will be close to 90% by the end of this financial year. Telephone installation work has been transformed by giving it to contractors, often former Telecom staff. Waiting time for installations is down from 6-8 weeks to 48 hours. It used to take, on average, several minutes' wait to get directory service. It has been computerised. The average wait is now 15 seconds.

Dramatic changes have been made to reduce cross-subsidisation in the pricing structure. The domestic phone rental charged by the Post Office was originally developed out of rates charged by the British Post Office in the 1930s. It had simply been scaled up ever since. Our system has been that you pay that standard rental. You then get all local calls completely free of charge. Businesses could tie up a local line for 24 hours a day, and pay nothing more than the standard rental.

On the other hand, this gift was offset by hugely penal rates for toll calls amounting to some \$400 million a year more than any fair or reasonable charge. The system was rebalanced by increasing residential rentals by about a third late in 1988, and by 7% late last year. Simultaneously, the price of toll calls has been dropped by an average 40%. Overall, the price of a basket of services including inland tolls and local services was reduced by more than one-fifth, in real terms, in the 12 months from September 1988 to September 1989. Telecom in Britain, going through a similar process, has cut real costs by one third over a period of nine years.

There have obviously been anxieties among groups who feel vulnerable to predatory pricing, if it occurred. So Telecom has now given undertakings that:

- It will in future aim to limit increases in the domestic rental to the rate of inflation or less.
- If charges are introduced for local calls in the future, an option will continue to remain open to householders to go on paying the standard rental without any charge on local calls.

In other words, we have an assurance that households are not going to find themselves paying more in the future, in real terms, than they pay now. Moreover, both of the assurances given make sound commercial sense, and can therefore be expected to stand the test of time.

As a result, a stage was reached this year when the Cabinet and the Caucus were able to agree that Telecom should be placed on the market for sale to the private sector.