

PRIVATIZATION OF BUILDINGS AND LAND:
THE CASE OF EL SALVADOR

by

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Privatization of Buildings and Land in El Salvador
by
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ABSTRACT

Privatization is a concern, in the world transition to market economies and management of real property portfolios (RPP) -- the building and land stock of a government.

For political and technical reasons the Government of El Salvador's (GOES) process of privatization is unlikely to occur in the near future, in ways that could recognize either the real asset value or the highest and best use of the real property held by public institutions/State Owned Enterprises (SOE's).

Literature on privatization of SOEs considers real property in only an incidental manner. No references were found regarding changes of use in real property held by State Owned Enterprises (SOE's). However, changes in real property uses, such as leaseholds, that have not been labeled as "privatization" have occurred for years in the public sector.

A proposed privatization with a real asset management perspective includes: consideration of the opportunity cost of holding real property; distortions such as free-space subsidies; exchange-value and use-value tradeoff; and complementarity among properties.

The GOES privatization initiatives include: a) the elimination of fiscal drain functions; b) the divestment of real assets to generate revenues for the budget; and c) the provision of land to squatters.

The case studies show that, the current GOES privatization process does not account for the opportunity cost of holding SOEs whose space has the following characteristics: a) underutilized subsidized, and/or surplus to the GOES's needs; b) non-intensive-uses in prime development areas; c) potential for a highest and best use other than the current use; and/or d) characteristics that enhance other candidates real asset value.

The GOES privatization program decision-making process responds to political pressures rather than technical arguments.

The three different initiatives of the program lack overall vision and coordination. The GOES privatization takes place in a context of widespread mismanagement of the public sector's RPP. This document proposes: a) to complement the current privatization evaluation with a real property asset management perspective; b) to centralize the decision-making process of the different privatization initiatives; and c) the improvement of the current inventory efforts.

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SUBJECT AND SCOPE

Privatization is an increasingly important phenomenon in the world transition to market economies and the reduction of the government's role in society. Privatization that involves publicly held buildings and land --real property-- is an important concern in the management of the total building and land stock of an organization --real property portfolio (RPP).

The key proposition of this thesis is that the process of privatization by the Government of El Salvador (GOES) is for political as well as technical reasons, unlikely to occur in the near future, in ways that could recognize either the real asset value or the highest and best use of the real property held by public institutions/State Owned Enterprises (SOE's).

This work shows why privatization that includes real property asset management practices is a better approach than the current privatization process.

No studies have considered privatization from a real property portfolio management standpoint according to the Laboratory of Architecture and Planning (LAP) at M.I.T. This thesis aims at advancing general knowledge in the field of real property asset management. In particular it seeks to derive lessons that can be used by other privatization processes.

BACKGROUND AND ACKNOWLEDGEMENTS:

This study was engendered in late-1989 after conversations with top government officials in El Salvador. It was suggested as a contribution to understand the government as a property owner with very different types of properties or investments. To this end, I appreciate the confidence and the collaboration that I found in the Foundation for the Economic and Social Studies, FUSADES, and the Department of Economic and Social Studies (DEES). I would like to thank the people at DEES, and especially Pedro Arriagada and Jose Marquez for their support and guidance in the effort to foster an awareness of the

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INTRODUCTION

The key proposition of this thesis is that the process of privatization by the Government of El Salvador (GOES) is, for political as well as technical reasons, unlikely to occur in the near future in ways that could recognize the real asset value of real property held by public institutions and State Owned Enterprises (SOEs). This thesis is organized into six chapters.

Chapter One, Introduction, describes current methods of privatization of SOEs current methods. It examines how those methods consider real property --land and buildings -- held by SOEs and show that real property is been considered as an incidental element in privatization analysis. It further examines why privatization with a real property asset management perspective can improve the achievement of the real asset value.

Chapter Two, Theoretical Framework, analyzes the following key issues in the analysis of the real asset value that could improve the privatization process: the opportunity cost of holding real property; distortions such as free-space subsidies; the exchange-value and use-value tradeoff; and valuation. It examines opposing views in the literature with respect to the achievement of the real asset value.

Chapter Three, introduces the different GOES privatization programs and the GOES's real property portfolio.

Chapter Four, examines two case studies of SOEs in light of the framework of Chapter 2. It shows the opportunities foregone under the current program of privatization.

Chapter Five: contains an analysis of key factors in the GOES privatization program that preclude the current process of privatization achieving the real asset value of the real property held by state owned enterprises (SOE's) and public institutions.

CHAPTER 1 PRIVATIZATION: BASIC CONCEPTS AND TECHNIQUES

This chapter describes the basic concepts of privatization and the most commonly used methods of achieving it. This chapter considers why it is important to consider an asset management perspective in the privatization of government-held real property.

The chapter has the following contents: first, it provides an overview of privatization in relation to State Owned Enterprises (SOE's); second, it examines privatization methods and considerations; third, it presents selected implementation aspects such as valuation; fourth, it introduces real property as a concern in privatization of SOEs; fifth, it explores how real estate has become a concern in the process of privatization; and sixth, it explores the potential relation of privatization decision-making and real asset management.

1.1 AN OVERVIEW OF PRIVATIZATION.

Changing economic conditions and the transition to market economies have influenced governments worldwide to redefine the role of the state in the economy, reducing fiscal and operating deficits, reducing the size of the public sector, and developing restructuring/adjustment strategies in order to achieve these objectives. In this context the top agenda of governments worldwide is privatization.

Privatization is defined as the process by which a government, at any level, progressively transfers the ownership and/or management control of government entities, assets, functions, and activities to the private sector.

According to Mary Shirley of the Country Economics Department of the World Bank, divestiture is a term that includes privatization. Divestiture is defined as: "liquidation, both formal and informal, whereby operations are suspended, but the State Owned Enterprise (SOE) ¹ retains a legal and economic life; privatization of ownership through the sale of the firm as a going concern of all or part of the firm as a going concern or

all or part of the assets; and privatization of management through leases and management contracts." [Shirley, v]

Privatization is a notion encouraged by important institutions such as the World Bank, the International Monetary Fund (IMF) and the USAID ². These institutions have been providing support and technical assistance to privatization and divestiture efforts, and an expansion of these areas of activity is envisaged [Vuylsteke, 2].

Privatization literature has until very recently been about SOE's or government functions. Real property ³ --land and buildings -- has been considered as an incidental element in privatization analysis of SOE'S. No cases have been found in the current privatization literature, where the real property has been the key factor, nor where the real asset value and the achievement of the highest and best use have been taken into account. (This notion is explored further at the end of this chapter).

In the last few years however, the term "privatization" emerged as a much broader concept, encompassing programs such as cutbacks in state activities to allow room for private initiatives; or the general reassignment of property rights from the state to the individual (as in Chinese agriculture or in Mexico where 28,000 farms in the form of ejidos ⁴ which occupy 1 million square kilometers --half of Mexico's total land area-- will be allowed to be privately owned by either the current farmers or potential investors [Economist, Nov 16th-22 1991: 49]. In the last few years it has meant giving land to squatters in Peru or El Salvador. A new approach to privatization resulted from the decision to privatize publicly held real estate in such countries as Russia and Hungary.

World Bank studies show that divestiture is a rising concern in the programs of structural adjustment in developing countries, for a number of reasons: [Shirley: 1987, 2-3].

a. The upsurge in interest in divestiture in the developed world, most notably in Britain, Italy, and France.

b. The sense that the state has become too large. divestiture reduces the burden of SOE's.

c. The hope that divestiture will lead to more imaginative and efficient use of resources.

d. The expectation of divestiture as a force for efficiency because financial transactions between government and private firms are expected to be more transparent.

e. The democratization of the national assets, Chile privatization program, for example, aims at increasing participation, partly to raise the public's awareness of and pressure for SOEs' efficiency.

f. The interest in raising revenues, for example privatization in Thailand, has been justified in public discussion by the argument of raising substantial revenues.

g. Privatization as a way to reduce fiscal pressures by getting rid of unprofitable SOE's through liquidation and sales

1.2 PRIVATIZATION METHODS

The main techniques and key characteristics are described by Vuyskele⁵ in Table 1. The choice of privatization techniques is generally a function of the government's objectives, the condition of the SOE, and its sector of activity, and the country's characteristics. [Vuyskele,3] Experience reveals that carefully modelled practical approaches can come close to satisfying both stated objectives and various types of constraints. Several combinations of the above may exist as well. Some governments (France, UK and Chile) have carried out a substantial number of privatizations using a broad mix of techniques. Some of these methods can bring about total divestiture or can be implemented partially or gradually. One must be careful however when choosing particular techniques, since they depend upon various factors, such as those described in section 1.22.

<u>Methods</u>	<u>Characteristics</u>	<u>Procedures</u>
Public offering of shares.	Distribution to the general public of all or part of shares in public limited company (as a going concern).	If SOE is in required condition, standard processing of public offering on the basis of prospectus. If not in required form or or condition, then readying process necessary. Offer can be on fixed price or tender basis.
Private sale of shares.	Sale of all or part of government shareholding in a stock corporation (as a going concern) to a single entity or group. Can take various forms such as a direct acquisition by another corporate entity or a private placement targeting institutional investors. Can be full or partial privatisation (i.e., transformation into joint venture).	Sale may result from negotiation or competitive bidding process. May be done <u>ad hoc</u> or may be subject to mandatory country procedures or guidelines on valuation, prequalification, evaluation of proposals, terms of payment, etc. In some cases, prior restructuring necessary. Involves investor search.
Sale of government or enterprise assets.	Sale of assets (instead of shares). Private sale.	Alternatives: sale of assets by government; disposal of some assets by SOE; dissolution of SOE and sale of all assets; other. Procedures for private sale of shares generally apply.
Fragmentation.	Reorganisation of a SOE into several entities (or one holding company and several subsidiaries.) Each entity will be then be privatized separately.	Depends on structure of SOE.
New private investment in SOE.	Primary share issue subscribed by the private sector (dilution of government's equity position instead of disposal of shares).	Public offering or private issue of new shares on basis of standard procedures for new issues, possibly in conjunction with disposal of government equity. New private investment may be for capitalization of new company embodying assets transferred by government.
Management/employee buy-out.	Acquisition by management and/or workforce of controlling interest in SOE. Leveraged management/employee buy-out (LMEBO) consists of purchase of shares on credit extended either by seller (government) or by financial institutions.	Negotiations by government, management, employees and lenders to cover wide range of issues.
Leases and management contracts.	No ownership transfer. Under <u>lease</u> , fee is payable to owner of productive facilities; lessee assumes full commercial risk. Under <u>management contract</u> , owner pays for management skills, while manager has full management and operational control. Many	No standard method; see actual cases in text.

Table 1. (Source Vuyskele: study for the World Bank)

1.21 Review of the methods shown in Table 1.

Method 1 and 2 Securitization and Sale

Under the first two methods of privatization, the state sells shares to the private sector, as if the enterprise were an ongoing concern. These methods are not evaluated since most of the developing countries do not have well developed capital markets which are necessary to support this approach.

Method 3. Sale of Government or Enterprise assets

Using this method, a government may sell the assets directly and/or the SOE's may dispose of the major assets. Generally, while the purpose may be to hive off separate assets representing different activities, it might also mean selling an enterprise as a whole. In some cases assets are not technically sold but are contributed by the government to a new company formed in conjunction with the private sector. The shares received by the government in this operation may be sold later.

The sale of assets can take many forms from a sale of surplus assets to a liquidation that requires restructuring of the SOEs. The sale of assets is the preferred method when SOE's are not saleable as ongoing concerns.

Method 4. Reorganization into Components Parts (Fragmentation)

This method permits different methods of privatization to be applied to different component parts, maximizing the overall process. If an SOE in the aggregate has various activities which are unattractive to investors, then fragmentation is an alternative. On the other hand, the State might want to retain some components of an SOE while selling others. British Rail, for example, in addition to its railway assets, first sold a portfolio of interests in other industries, such as ferries, hovercraft, hotels, and surplus properties. When facilities that are attractive to investors are not part of the main business line, they can be easily disposed of.

Method 5. New Private Investment in SOE.

This method might be used when a government wishes to add capital to an under-capitalized SOE for their rehabilitation or expansion. Therefore the state does not dispose of its current equity, but sells additional equity to private investors and dilutes the government's equity position. This might result in joint private/government ownership of the enterprise.

The state might also provide the assets as the contribution to a new venture. In the case of existing SOEs this would permit physical rehabilitation or expansion of operations. This is a preferred method when a sudden sale of government assets might be politically difficult to carry out (or if the government wants to secure the property of the assets). At a later time, once the transformation has taken place, a gradual transfer of government ownership could take place more easily [Vuyskele, 28].

Method 6. Lease or management contracts.

Under this scheme private sector management, skills, contracts and arrangements are provided under contract to an SOE or in respect of state-owned assets for an agreed compensation and period of time. There is normally no ownership transfer, and no total divestiture of the publicly held assets. A lease arrangement might increase the effective use of the state assets. This method might improve the future prospects of improving the SOE which could be divested at a better price. There are two mechanisms:

a. Lease. The private sector leases facilities owned by the state and uses them to conduct business on its own account [Vuyskele 36]. The terms and conditions for the lessee to operate the assets or facilities, the compensation to the state, and the parties' responsibilities are set in the lease. A feature of this arrangement is that the lessee assumes full financial responsibility for operating the assets. The lessee has control over the operations of the assets or facilities

(subject to maintenance and repair covenants), and the government has the authority specifically granted under the contract (For example the lease a hotel in Gambia to a hotel company). This sort of arrangement is recommended in cases such as the Soviet Union where there had not been transactions in the past so there are no comparable sales to value the SOEs' assets.

Even if not acknowledged by the current privatization literature the public sector was involved in these kinds of arrangements before the term "privatization" came into fashion. These efforts were known as public leaseholds and they are discussed in section 1.5. Other examples of joint-ventures include non-profit institutions such as universities which provide surplus land to the private sector in order to develop research parks, or office space. In these cases such institutions because of their long-term horizon, want to secure land, but at the same time they assure that the land produces an income. In some cases, its development increases the land value and economic activity in the area as an added bonus.

b. Management contract. The contractor, is normally a company in the same line of business of the enterprise who assumes responsibility for the operations. Whereas a lessee pays the state for the use of asset or facilities, the management contractor is paid for its skills. Management contracts are widely used in the publicly held hotel sector.

Lease or management contracts are the preferred method for privatization of an activity in cases when it might not appear appropriate to divest the assets. This might make in certain cases their application preferable to other methods of privatization. The lease could also be an interim solution previous to a sale. A management contract or a lease, rather than a sale, is the most desirable method in some instances. The lease is a preferred alternative if all the operations of an SOE have ceased, or a run down SOEs is unlikely to respond to private management expertise [Vuyskele, 40]. This is a recommendable solution if a government, which has a long time

horizon, wants to secure the property of the assets for the long term while getting revenues meanwhile.

1.22 Determinants of Potential Techniques.

The methods of privatization are determined by:

a. The government's objectives. The economic strategy of most governments provides for a combination of objectives. For example, if a government looks for greater revenue from state assets, this objective leads to methods that can maximize the sale price. However this cannot be possible in all countries.

b. Financial conditions and record of performance. The profitability in terms of revenue generation or budget drain of the SOE is a key determinant of the degree of difficulty for its sale or its identification as a potential candidate. The potential SOEs are not limited to high performing companies. Loss-making SOEs could be privatized through a variety of techniques; however restructuring measures are normally necessary such as physical rehabilitation. SOE's in developing countries are often without adequate records, have over-valued assets, and have lacked financial discipline as shown in the exhibit I.

c. The linkage of the SOE sector of activity to the economy and its importance for the government. Once the government has assessed the fundamental objectives for which enterprises were created and determined whether if these goals are still valid, it should decide which enterprises should remain public and which should be privatized or liquidated. Governments tend to classify enterprises as "strategic", "core" and "essential" or "non-strategic", "non-core" and "unessential".

d. Degree of development of the capital market. If, for example, there are no channels for share distribution and the investing public is small then private sales to local and foreign investors are likely to be the predominant method of sale.

Exhibit I Typical Characteristics of SOE's

Management.

- * Lack of accountability at all levels.
- * Operate outside the Government budgetary process.
- * lack of accurate or up to date financial records.

Physical.

- * Under-utilized assets and inadequate planning feasibility studies for new investments.
- * Overvalued assets, accompanied by an unwillingness to recognize market value.*
- * Poorly maintained capital equipment.
- * Antiquated production facilities, procedures, and technology

Operational.

- * easy acceptance of financial losses for social reasons.
- * Over staffing.

Source [USAID, Guidelines for Privatization, 8]

* (note) In some countries of the Eastern Bloc assets are referred to, by other literature, as being under-valued.

e. Socio-political factors. The decision-making process is normally intense in political terms. However some methods might offer alternatives for dealing with pressures.

Once these factors have been considered, most governments aim at identifying strategic enterprises which need rehabilitation and are likely to remain in the public sector for some time. In most countries no more than 10 or 15 enterprises are in this group. They include electricity, water, post and telecommunications, railroad companies, and some mining and industrial firms that cannot be easily privatized because of their link to the economy. [Shirley, 1989: 37]

Governments would be wise to then let the remaining SOE's to begin to fend for themselves [Shirley, 1989 :37]. The government must decide whether the non-strategic enterprises will be sold, liquidated, or rehabilitated. In order to do this the governments should clarify the SOE's true situation, by eliminating gross price distortions, cutting most subsidies, and

halting most new public investments. If price distortions are few, the cost and benefit of rehabilitation and continued public operation can be more easily determined. Most entities will have to be categorized in term of their potential to earn a positive return, as well as in terms of the way such enterprises commonly operate elsewhere.

This thesis proposes the suspension of space-subsidies. Space subsidies are the space provided free of charge by the government to its institutions/SOEs. Providing free space subsidies to SOEs distorts their financial performance evaluation. This prevents consideration of real asset value, since no pressure to evaluate the usage efficiency is created.

Most entities should be categorized by their earning potential, the way private enterprises commonly operate.

No free subsidies in the form of land or facilities should be given to SOEs that offer services for sale or lease to third parties. Return must be generated on the invested capital of these entities. Otherwise they might be subsidizing very limited groups. The last buyer, for example, will acquire the goods or services at a price lower than it costs to produce them.

1.23 Overview of the experience with privatization.

The examination of the World Bank literature above has shown that divestiture programs need to be tailored to the circumstances of the particular country. For example, in small economies with limited capital markets, methods such as liquidation (see page 2), contracting out, leasing, and management contracts may be more effective than sales in restraining an overextended public sector.

Privatization has taken drastically different forms in different countries. Which are the best methods for each specific case? Considering a portfolio or even individual properties, different methods can be used. In Sri Lanka and Malaysia, creative approaches that combine most methods have been

developed such as combinations of leases/private sales/public offerings. In Malaysia's Port Kelang, a joint-venture was arranged to lease the relevant assets and acquire the container business from the government. In the Soviet Union as in some Eastern Europe countries where there have been no real estate transactions, the estimation of real estate market value is difficult and inaccurate. In these case a method recommended by Tim Larson consultant on Privatization for the Russian government is long term lease or joint-venture. This method permits the state not to dispose of the property now while generating benefits and economic activity. This way the state participates in the potential appreciation of the land. However the use of this approach may be problematic in a country in desperate need of cash.

In assuming the potential of its enterprises, all elements should be considered fully. Companies and assets may occupy attractive market niches which are presently underutilized or neglected, such as the case of some British Rail subsidiaries.

1.3 SELECTED IMPLEMENTATION ASPECTS.

The literature of the World Bank acknowledges that privatization programs must account for the different types of rationales governments might have. Privatization is a relatively new and experimental activity. Governments of developing countries, may not have all the necessary conditions for success. Some lessons that the World Bank has drawn from divestiture programs for less developed countries are: [Shirley: 1989, 34-36]

a. Divestiture should be treated not in isolation or as an end in itself, but as part of a broader program of reforms, which could aim at promoting better allocation of resources, encourage competition, and develop capital markets.

b. Work is needed to improve the environment for privatization and to strengthen government management of sales.

c. Transparency. A debate about the privatization merits is inevitable. The challenge is to make the debate an informed one. More should be known, for example, on how much subsidizing goes on the SOEs. Benefits have to be added to the debate if acceptance to the privatization program is desired.

d. The immediately visible social implications of plant closures and lay-offs can be severe in the short-term while the growth of benefits and increases in employment and investment do not appear until later.

e. The design of a strategy for divestiture and the classification of SOE's to be liquidated, sold, leased, and so on, have been useful in clarifying the government's objectives and approach. However, the more comprehensive the approach, the slower the process is likely to be, and the more costly. The formal scheme may interfere with informal closures if authorities feel encouraged to maintain the operation of SOEs in a possibly vain attempt to sell them. Care should be taken not to replace informal actions with formal commitments.

The organizational capability and technical expertise must be present in order to initiate and implement the transaction. Every privatization undertaking needs to be carefully planned and managed. When designing an action plan, it is advisable to assess the respective merits of alternative techniques. In most cases, minimum standards or guiding principles must be conceived to ensure a proper disposition, to maximize the return to the state, to preserve a fair process for the general public, and to assure that the purchaser is qualified to run the acquired enterprise productively. According to Vuyskele, implementing privatization implies the following:

1.31 Planning and management.

A country needs to be clear in advance about the initial steps to be taken, and have identified some initial viable candidates. Planning and management includes the following:

a. The selection of the first enterprise or enterprises

for privatization through sale is key, "as its success or failure will influence the future of the whole privatization plan". The strategies for choosing the first candidates for privatization may be determined by various socio-political factors. In the case of Egypt, the first privatization addressed hotels, as these perhaps do not as greatly concern the population at large.

b. A state may do well divesting gradually its assets even within a single enterprise.

c. The legal environment influences to privatization. In the UK, the privatization process was delayed due to the need for separate pieces of legislation for each part of the process.

d. The administrative structure must be responsible to the interests of government, interested business circles and investors, and other relevant parties. Governments must remain flexible be flexible and allow for ad hoc solutions.

e. The procedures for privatization should safeguard the public's interest. Private sales particularly should be subject to minimum standards that ensure orderly disposition, maximum return to the state, a fair process for the general public, and assurance that the purchaser is qualified to run the enterprise.

In this case the government may agree with the investor as to which kind of solution this would involve, or set limitations. This notion could be linked to the possibility of inserting rigorous conditions for the unbiased valuation of assets and for determining the sale price. In the absence of such rules, irregularities of different kinds may arise and result in not getting a fair price.

f. The general business environment is fundamental to the success and sometimes to the feasibility of privatization.

g. A detailed action plan should follow the announcement of privatization. This should include: objectives, timing, financing, valuation of companies, studies of adjustments and prior changes that can increase the possibilities (and/or) price

of the sale and identification of potential privatization candidates.

1.32 Readying SOE's.

Normally few SOEs are in a condition that permits sale of land or other transfers to the private sector without readying measures. No format exists for private sales, which may range from a restructuring of the company prior to sale as an ongoing concern to a liquidation following a disposal of assets. Physical rehabilitation is a concern of this study. The question is, should necessary physical rehabilitation be done prior to privatization?

From the standpoint of the consideration of the real asset value the decision of selling the enterprise in its present condition is difficult, as its potential value may not be realized and leaving the government open to criticism for disposing of the national assets at low prices. It is conceivable that physical rehabilitation may increase the sales potential of the enterprise and permit the cost to be recovered. However, as a general rule, rehabilitation of assets prior to the disposition should be avoided.

1.33 Valuation and Pricing.

The need to maximize potential revenues must be balanced in determining the conditions for sales. The highest price will not produce in all cases the best benefits. For example, even if a transaction (say for a social reason) might yield a low price, it might be right if it addresses the government's economic, political, and social objectives.

However even the "best price" is not always the best price. The pricing of a given SOE must be carried out in the full context of a broader privatization's program and government's objectives. It is more important to gain an "aura of success" than getting the last penny, this can increase the benefits of the whole program in the long-term. Experience shows that is

better to err in the side of a "too low price than too high" in view of the high cost of an operation that fails. [Vuyskele 115]. For the purpose of selling assets (or shares) valuation and the resulting pricing are sensitive and difficult matters. In most case such as France or UK companies' share prices increased too fast and the government were attacked for selling too low. "While a too low price might create a criticizable windfall of investors, however too high a price might entail a failure of the privatization effort." [Vuyslkele 110] The experience of Great Britain shows that for political reasons shares in SOEs being privatized are commonly underpriced in the initial sale. This results, in the new shareholder benefiting at the expense of the whole country. [Vuyskele,] Public assets sold directly to predetermined companies or investors rather than by public offering involve the risk of political favoritism and underpricing [Starr, 9].

Only very rough guidelines can be set for SOE valuation. There are so many different circumstances that any delineation of the required measures for valuation cannot be set. (This notion is very important in the context of Chapter 2, which analyzes issues related to the achievement of the real asset value.

Methodologies such as discounted cash flow are based on forecast of future performance and expectations of value earnings and better capture the variety of different factors that valuation should take into account. In assuming the potential for enterprises, real property elements should be considered fully. e.g companies and assets may occupy attractive niches or are underutilized.

In some countries the valuation must be carried out using objective methods that are applied consistently with respect to the sale of company assets. Serious efforts should be made to establish the economic value of the assets, especially those that appear to be overpriced acquisitions.

In general, countries need to develop an approach for

valuing enterprises or assets with sufficient flexibility to permit the establishment of a price that corresponds realistically to the level of interest in the private sector. As to private sales of shares assets, one approach is competitive bidding or an auction with a price determination in line with the enterprise's or asset market value.

1.34 Determining Future Ownership.

What is the level of private ownership desired in each case (partial vs total privatization). The transfer at various degrees of ownership depends on government objectives and market conditions. Partial ownership has been maintained when there is a need for control over some sectors of the economy, or just to increase efficiency, or when there is a need for gradual privatization. Partial privatization results in joint state-private companies. This introduces the risk to private investors, who have fears about government involvement. Promoting ownership has been an objective for many privatization programs. Removing the old distinction between owners and workers such as in the case of Chile. The divestiture programs of Peru and El Salvador include the distribution of the ownership of government land among squatters (see section 3.4).

1.4 REAL ESTATE IN THE PRIVATIZATION OF SOES

The analysis of real estate is basic to privatization evaluation as described above because of the following:

a. Real estate components, land and buildings, are capital goods that, together with other production input, labor and capital, form the capital combination underlying a production plan.

b. Real property is the most valuable but often a wasted form of assets. On average, 30% to 50% of a corporate total assets are real property, and this percentage is much higher in the public sector. [Chai, 2]

c. Real property is an important component of the SOEs'

assets and the government's real property portfolio (RPP).

d. The state-owned sector in developing countries tends to be large, diverse, and illiquid [Shirley,3]. Real property assets of SOEs are often under-utilized (see exhibit I).

1.5 PRIVATIZATION PROCESSES THAT INVOLVE REAL ESTATE.

Real estate is increasingly becoming a target of privatization programs, especially given the impending transformation of the Soviet Union and Eastern European countries to a market economy. Most of the real estate inventory of Moscow, for example, is currently owned by the State. This inventory includes factories, housing, commercial buildings.

According to Tim Larson, a consultant for the Russian Government, Russian authorities are seeking pragmatic methods for real property privatization. They want to privatize quickly given their need for money, but only few investors willing to provide capital. Leasing assets, either in form of assets for ongoing use or for development of real estate might be a good alternative, given the absence of past real estate transactions. Leasing has two advantages: the State may create value on its land and generate new businesses in the land.

The U.S. public sector at all levels has either disposed surplus property and assets of various commercial enterprises or contracted out various services to the private sector before the labeling of the word "privatization." However, most of these transactions have not been acknowledged by the privatization literature. Some examples include:

a. The Charlestown Naval Base, an old U.S Navy facility in Boston was developed in a joint venture between a private developer and the State.

b. Public leaseholds created when a public body owning land leases or rents to a private individual or firm, for a specified period of time. One of the most frequent proposals for tenure reform is that most developable urban land be held in

this type of tenure. Some features are that "Leasehold will provide sufficient security of tenure to allow and encourage good building provided that the lease period is not less than likely minimum economic life of the building and provided that the land rent is not greater than the market value of the site in its current use." These periods, however, can be very long, Archer recommends a range of 60 to 120 years, with a common leasehold being 99 years. Given the rapid growth rate of today's cities, such time periods become, for practical purposes, virtually the same as freeholds, unless the lease itself gives certain kinds of residual controls to the public lessor. However, the greater the degree of public intervention possible, the less attractive the lease may be as collateral for credit being given to the lessee. The use of leasehold puts a public authority in an excellent position to adapt to changes in urban form and land use patterns. As leases expire, the property can simply be released to a lessee who agrees to convert to the use most appropriate to the changed circumstances. The 60-year rhythm of renewal is far too slow for the rapid changes in urban form particularly in the developing countries. One may generalize that the suitability of many structures and uses in the older parts of cities in developing countries will require major functional adaptations on a cycle closer to 20 years than 60. Surprisingly, leaseholds have not been treated nor referred to by the privatization literature.

c. The sales of public assets, including public lands, public infrastructure, and public enterprises is another privatization concept gaining importance. Some public assets are easier to privatize than others.

. The U.S Postal Service owns prime located real estate that and could be used more productively. In its restructuring it could sell assets such as downtown distribution centers next to railroad terminals. (resulting from the time when a lot of the mail went by

rail). This situation contrasts with the situation of a competitor, United Parcel Service, that has located its facilities in less valuable suburban locations.

. Railroads are one example of companies that have discovered the immense value of their real estate, e.g the Santa Fe Pacific and its Catellus Development Entity. In Boston, for example, the railroad holdings in the North End sector could be leased for utilization of air rights over the tracks.

. Housing is another potential area for restructuring public assets. Unlike education or justice , housing is not a service that Americans believe government should produce and manage. Public housing projects could be sold to tenant cooperatives. In such areas as housing the government could move its investments in a "rolling privatization" disposing of some public assets while augmenting others [Starr, 16].

Given the rising acceptance of "privatization", the above approaches are currently recommended as a thorough solution to the aforementioned problems of government. These approaches serve as background to the consideration of alternative uses to the current use in government real estate assets held by obsolete SOE's/entities, in order to fully realize their real asset value and highest and best use.

Public owners of real estate considering privatization may dispose of current assets while acquiring new assets as mentioned above. This is a concern of real property asset management (RPAM), a strategic concept, which involves the entire real estate assets of the public sector. The comprehensive management of all real property, buildings, leaseholds, contracts and land is included. RPAM provides an overall vision for decisions such as disposition, privatization, acquisitions and/or rehabilitations [Isacson, 26]. RPAM aims at searching for a fit among changing real estate characteristics

and needs of the owner/user with the shifting market forces which drive the economy and the particular organizations, in order to satisfy the need for land and buildings [LAP, 1986: 60].

1.6 PRIVATIZATION WITH A REAL ASSET MANAGEMENT PERSPECTIVE

Privatization was previously identified as a topic of interest for real asset management in an unpublished paper of the Laboratory for Architecture and Planning (LAP) at M.I.T. In 1986, the LAP identified privatization as an option that managers and owners of public real property have. The LAP recommended also that this option be researched. As of today no research, has been found with this emphasis.

Privatization as an option in real property asset management, as suggested by the LAP, raises the following concerns:

a. Privatization has taken place in recent years as the chief agenda of many countries worldwide.

b. The complex character of the privatization decision process implies the consideration of multiple factors other than real property concerns.

c. Privatization has been taking place independently of real property management. Most governments do not have adequate real property management structures. Existing real property management in public institutions only accounts for historical costs of real property.

d. Real property asset management, regardless of its theoretical and practical importance, has received little attention in both corporate and public settings. RPAM practice has traditionally been ad-hoc, reactive, and short-sighted, partly as result to a lack of a supporting body of knowledge [LAP,]. Real property managers in public settings do not participate in the strategic government decision-making.

This study emphasises the importance of complementing the current privatization analysis by taking into account real property asset management practices in order to improve the current privatization process. It is essential to identify theoretical and practical evidence that real asset management practices would improve the privatization process outcome.

Privatization and real property management literature assign importance to the consideration of the real asset value (see section 2.11). The valuation of the real asset value is a key concern for both real property management and privatization. However, contradictions that appear in the procedures for achieving this value in the transactions (see section 2.27) result in the real property real asset value being generally ignored.

SUMMARY OF THE CHAPTER 1.

This chapter provided an overview of current privatization practice. It introduced the basic concepts of privatization and divestiture, and discussed the most used methods of privatization. It showed that the analysis of real estate as a component of the assets of the SOE to be evaluated is basically related to issues of valuation. Further discussion centered on these assets were privatized as ongoing concerns. Few examples could be found in the literature of privatization that treat the experiences of assets sold as real estate. No examples were found to document changes of uses in the real property of the SOE's, nor of SOE's identified as potential candidates for privatization because of their potential highest and best use as opposed to their current use.

NOTES OF THE CHAPTER.

1 Divestiture has been linked to the State Owned enterprise, which can be defined as a publicly owned entity with a separate legal personality that earns the bulk of its revenue from the sale of its goods and services. Implicit in this definition is the potential for the company to earn a return on its assets.

2 According to the World Bank , government initiatives in the privatization of State Owned Enterprises (SOE's) and publicly held assets have increased substantially in recent years. In at least 83 countries, privatization is the key procedure to rationalize the SOE's sector in order to reduce its burden on the fiscal deficit and improve its efficiency.

3 The term "real property" refers to land and buildings denoting their exclusive use, ownership and disposition. [Bon, 1988:] Real property includes all the interests, benefits, and rights inherent in the ownership of physical real estate. A right or interest in real property is also referred to as an estate. [AIREA, 1987: 5]. Real estate is the physical land and appurtenances --buildings and improvements-- affixed to the land-- attached to it by people. One must start defining these two concepts since some of the literature calls these two terms indistinctly.

4 The ejido is a purely Mexican idea, whose origins predate the Spanish conquest. In 16th-century Spanish the word simply meant common land. In its modern form the ejido system arose out the peasant insurgency of Emiliano Zapata and was institutionalized in the 1930s by President Lazaro Cardenas. [The Economist, Nov 16th 1991, 49].

5 The possible approaches to privatization and the attendant issues are covered in detail in Charles Vuyskele, "Techniques of Privatization of State-Owned Enterprise," Vol 1 World Bank Discussion Paper 4, Nov 1986.

6. Public Freeholds. This category applies when a public body is full owner of the land. In urban contexts, it generally refers to land directly used by the public, such as parks, roadways, sites of public buildings, etc. In a national context, it is common for the national Government to own vast areas of the country in various kinds of forest, conservation, mineral, recreation, or other types of reserves. These themselves may have special names, such as baldios in Latin America. In Mexico a very substantial portion of the country is in ejidos, a form of national ownership, but which clearly defined rights of occupancy and use by small farmers (ejidatarios) [Archer, 47].

CHAPTER 2. THE A REAL PROPERTY ASSET MANAGEMENT PERSPECTIVE IN THE CONTEXT OF PRIVATIZATION.

As discussed in the Chapter 1, a real property asset management perspective is most important for privatization. Chapter 2 now focuses on the principles of real estate analysis for a privatization decision-making that takes into account sound real asset management practices. These elements include particularly the achievement of real asset value and related issues. It further presents some guidelines that account for these concerns.

2.1 REAL ASSET VALUE ISSUES.

2.11 The Achievement of the Real Asset Value

The real asset value of real property is normally identified as the maximum value obtainable in exchange, the market value. Market value is defined as the highest price which a property will bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimuli. The market value estimate is based on the analysis of all relevant economic factors considered in the three valuation methods mentioned below, and on the highest and best use of a particular piece of real property. According to the real estate appraising theory three classic approaches are designed to reflect the respective sales (comparison analysis); economic (income analysis); and physical (cost analysis) characteristics of the subject property (see section 2.24).

According to the privatization literature examined in Chapter 1, real asset value can not in all situations be achieved. It does however, provide an important benchmark that should be evaluated continually.

2.12 Highest and Best Use

Highest and best use is defined as the logical, legal and most probable use that will produce the highest net return to the land over a sustained period of time. The principle of highest and best use is an important concept for valuation. For valuation purposes, the evaluation of the highest and best use is of importance in the relational analysis within the valuation three approaches. The accuracy of the valuation is related directly to the appraisal conclusion on highest and best use.

2.2 CONSIDERATIONS IN RELATION TO REAL ASSET VALUE.

2.21 The Consideration of opportunity costs.

Valuation of costs is impossible without an explicit account of opportunity cost --the satisfactions foregone [Bon, 1990: 61]. Opportunity cost is the value foregone in having one prospective opportunity displaced by the decision to take another course of action. According to Buchanan [1969; 28] "Any profit opportunity that is within the realm of possibility but which is rejected becomes a cost of undertaking the preferred course of action." The only sense in which cost can influence choice is the perception at the very moment of choice of the satisfactions foregone. For example, the choice to hold under-utilized real property, has an opportunity cost. This cost is determined by the difference of the amount the government is saving by choosing this option and the profit the property could generate if the property was rented or sold in the open market to a third party. The residual are the satisfactions foregone since the funds could be invested in something else. Say a real property produces 40 dollars monthly, but there are other alternative uses that can generate higher revenues on the property. The highest and best use would generate 120 dollars monthly. The differential between the two is the opportunity cost of the choice of holding the property in its current use. Privatization analysis should consider the opportunity cost of

holding real property; the management actions not taken; and the opportunities foregone.

The concept of opportunity cost is independent of whether the land or any other assets are privately or publicly owned. The conception of cost is the same. However, the actual measure of the opportunity cost varies according to the institutional structure, since the restrictions and opportunities differ.

The concept of opportunity cost is essential in large public institutions whose main activity is not real estate business but who are owners, tenants, or renters of vast amounts of real property. Regardless of their willingness to accept it, these organizations are related to the real estate business. [Ebert, 62]. These organizations do not regard their real property as having an investment potential hence sacrificing a possible income.

2.22 Changes of use in real property

In any economy, at every moment some buildings and other capital goods are utilized for purposes distinct from the one originally intended¹. Privatization analysis should account for the changing use of real property occupied by SOEs/entities in relation to changing economic conditions. Economic forces influencing public organizations affect the patterns of decision making concerning the investment in, divestment and changes of uses of buildings and land. This dynamic should respond to what the market decides is the highest and best use of a particular piece of real property.

Consideration of this dynamic contrasts with the current privatization processes where the buildings and land occupied by SOEs remain in their use regardless of the fact that its highest and best use is different from the current one. This distortion is due to the fact that public organizations ignore the opportunity cost of holding real property. They also ignore the distortions created by subsidies in the form of free space to their SOEs.

2.23 Useful life vs Economic life.

A useful benchmark for measuring the changes of real property in relation to the changing economic conditions is the tradeoff of the useful-life vs economic-life. Economic life is a function of economic viability. It denotes the period during which the improvements on a specific site are capable of producing a fair return on the land value. Useful life denotes the period over which a facility can be economically competitive and functional for use as designed [Albritton, 85].

These two conditions of buildings in relation to land must be continually evaluated in order to achieve the highest and best use of real property and therefore its real asset value.

Real property improvements might reach the end of their economic life faster than their physical life. This is illustrated by the concept of real property cycle ². The distinguishing feature of land in this context is the longevity of the asset. Land is a truly a non-depletable resource, whereas buildings wear out in a few years. Values of land and buildings change at different rates and/or in different directions, depending on the economic forces which influence them.

To illustrate the economic-life and useful-life tradeoff in a privatization situation, one could draw the following hypothetical situation: an SOE may use a relatively new facility which could be physically expected to serve its needs for many years and therefore have a long useful life. However, this facility may be located in an area that is experiencing rapid land value appreciation and therefore may not be capable of producing a net income sufficient to satisfy a reasonable return on the land. At this point in time, demolition/conversion/use-intensification of such a facility and/or redevelopment of the site should be considered by the government. The SOE function, if feasible, should be relocated (see Case Study 4.2). For a privatization analysis that considers a sound real asset management perspective, the useful-life versus economic-life

tradeoff is important in the following situations:

. In the identification of potential privatization candidates which are only selected based on their impact on the fiscal deficit in current privatization practice.

. At the point in time when an SOEs' real property economic life has expired regardless of its useful life, different alternatives should be evaluated such as conversion of use or divestiture.

2.24 Implementing Valuation considerations

Valuation considerations in privatization were introduced in chapter 1. This section expands some of those concepts. Privatization practice should carefully treat the concept of valuation. Some important factors in valuation in order to achieve the real asset value in privatization are:

a. It is important for the Government to achieve systematic knowledge of its current real estate holdings and their values as a means of achieving value maximization. Privatization candidate selection and decision-making could be improved if it had access to accurate information regarding the real property assets of the government and the real property occupied by the SOE's/entities.

b. Based on the experience of many countries, only rough guidelines can be set for SOE valuation in privatization analysis. There are many different circumstances and characteristics of assets and any delineation of the required measures for valuation cannot be set [Vuyslsteke, 111]. There are, however, important factors that could improve the valuation of the real property components of the privatization candidates and provide alternative criteria for their potential identification.

Privatization and real property management use the same three basic approaches for estimating fair market value:

1. The market approach estimates the market value of a subject property based on a comparison of the prices paid in actual market transactions and on asking prices for currently available assets. The market value approach may present two problems:

a. The comparable sales are liquidation transactions. Experienced owners or realtors would not expect to sell under in hard times. However, some governments undergoing privatization processes are in a hurry to get revenues. A massive divestment may create a liquidation climate.

b. There are not enough comparable sales in the market. The market approach is often hard to use since there might not be enough, or any, transactions in the marketplace. In this case the market approach can be a troublesome parameter if used for establishing the price of an enterprise or asset. In the Soviet Union, for example, there have been no volume of market transactions in the past 80 years. Therefore, the determination of market value creates a problematic issue for the government and for potential investors. On the one hand the government expects to get more from its property, but on the other hand there might not be potential investors with enough investment funding willing to pay such price.

2. The income approach simulates the economics of a particular property and can be most useful if the appraisal subject has the potential for rental or sale, as does an investment property.

It involves the capitalization of anticipated net income or cash flow projections and discounting them for the time value of money to indicate a present value. In addition, a present value of the projected residual value must be estimated and added to the present value of net income. The income approach sometimes distorted when an enterprise is under bad management or when financial losses are accepted for social reasons. Then there is the problem of governments trying to keep the enterprises running regardless of the real property highest and best use.

3. The cost approach stresses the physical characteristics of the improvements and economic value of the land. This approach uses replacement as an indicator of value. In privatization practice there is a trend to evaluate market value by replacement cost, e.g the case of Poland. This situation is explainable since governments want to get back what it is supposed that the State paid for a particular investment, or else there is a perception of potential problems arising as a result of accusations of giving away the assets. The problem, according to James Stephenson from USAID El Salvador, is that the replacement cost approach tends to overvalue many of the enterprises.

The replacement cost should just be considered if the institution being closed is critical to the state and cannot be operated by the private sector. Otherwise, the consideration of replacement cost is important only for the new private entity, not for the government. The rationale for this is the fact that the government is interested in evaluating the use-value exclusively for itself as the revenues an enterprise reports. The use-value for society is important, but it is the same since it can be provided by the private sector. There is a sacrifice that must also be made, related to the beneficiaries of each enterprise. They must be as well considered but its determination is out of the scope of this study. The exclusive use of the replacement cost approach, with no determination of the space needs of the future organization, may fail to detect the under-utilization typical of that created by SOEs for practices such as subsidized space. From a government standpoint, it would be better to consider market value when analyzing an entity for its worth to the government. Finally, improvements represent sunk costs from an economic view, so are irrelevant in estimating current value.

2.25 Use Value and Exchange Value.

Real property may have both a use value and a exchange value. According to Marc Louargand Value in use is the true worth of the asset to the owner/buyer/seller. Owners and buyers estimate this value on an ex ante basis. Their estimates compete in the market place to form the Value in exchange. If value in use to one particular owner is lower than to others the value in exchange becomes the predominant form of value.

For the practical purposes of this thesis the value in use for a particular government is determined by its estimate of net present value (NPV) of the revenues a given piece of real property could produce, given its current use in the production of income or services. For this piece of real property there may be investors willing to estimate the worth of the asset in uses different than the current one. Their estimates --together with those of the government-- compete in the market place to form the value in exchange. The value in exchange is therefore deemed as the market value.

Speculative buying and selling may drive up the price of real property, and this price may then determine the use by setting the lower limit on the income stream that could be obtained from the products it helps produce.

For example, an older government facility is located in an area where increased number of real estate transactions have driven up prices of real property. Since the output revenues that this particular property in its current use could produce are unaffected, the value in use for the government keeps the same. However the exchange value rises since there are investors who would be willing to consider this real property for other more profitable uses.

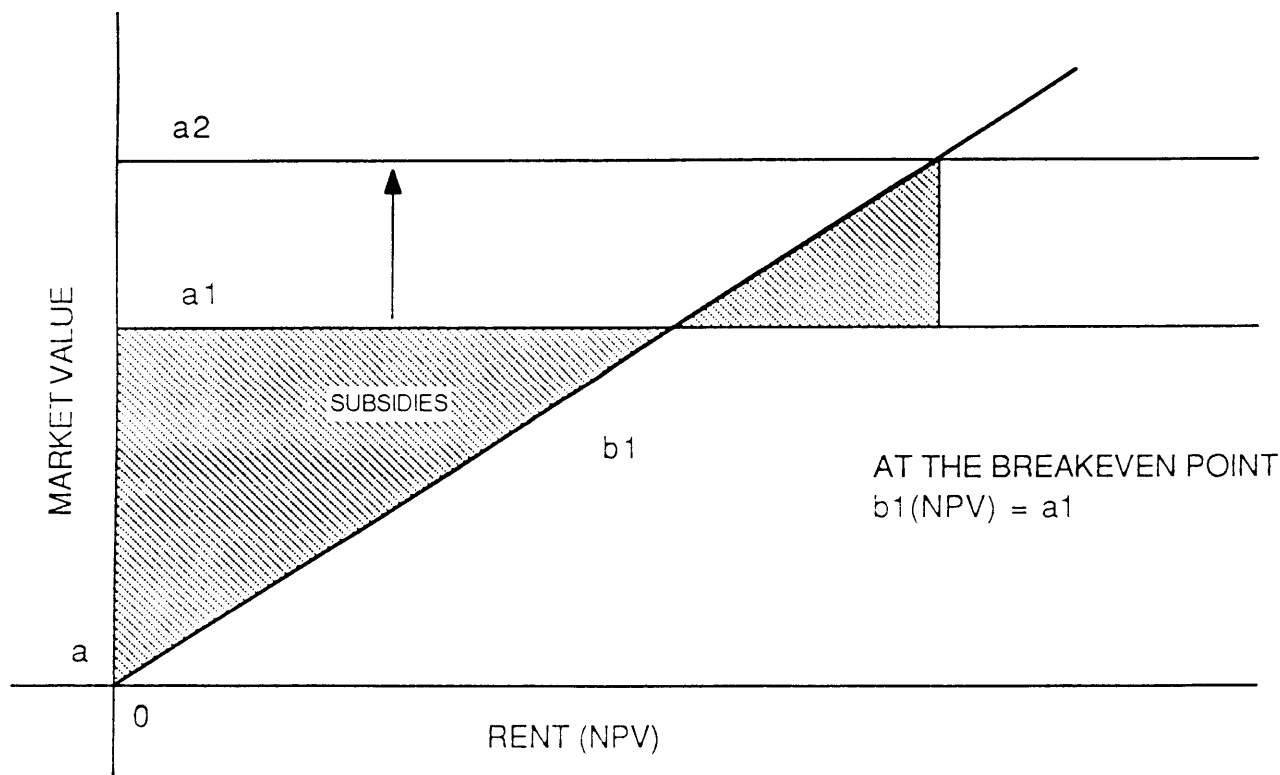
The decision to sell or keep a particular good, or a portion of the good will depend on the comparison of value in use and value in exchange. Ideally the use value should always be higher than the market value or the two should be in equilibrium. This means that in order to keep a property the

value in use for the owner should be higher or at least the same as the market value, that should reflect the expectations of other actors in the marketplace.

The relationship between use value and exchange value of a good is by no means static. It changes with changing economic conditions. Some of the causes of change in this relationship are: a) changes in the owner's preference structure; and b) changes in the properties [Bon :101].

The following model suggested by Marc Louargand compares use value for the government on the land as the rent it can bear vs the exchange value denoted by the market value.

If one sets the graph in which axis X is rent for the government, and axis Y is market value of the property. Line a1 denotes the actual market value of the property. Line b1 shows the rent that an enterprise could give to the state.



The following are two applications:

a) The determination of whether space is being subsidized. The property is subsidized if the rent is below the market value of the area. This would imply that the property is not in its highest and best use. If the rent is at or above market value, then the enterprise is profitable and the space is not subsidized. A property in its highest and best use could produce the second line in the graph.

b) To evaluate the possibilities of providing initially rent free real property in order to generate investors. Once the enterprise starts generating revenue, the company will start paying rent to the state. This would last for a determined period of time. Then if the enterprise reaches or surpasses the break-even point, it will pay rent above the market. In the meantime the property market value may have gone from a_1 to a_2 , in which case the user may be asked to buy at the new price of the property.

The model might be used if the State wants to give impulse to new enterprises which would not invest in land, but is progressively going to render the state a rental amount. The State will decide in the future to sell or retain the property as the need for space at that particular point in time shows.

2.26 Complementarity.

The complementarity among properties refers to the fact that some properties may be necessary to fully utilize other properties and/or enhance value of other properties. For example, an office building might not be utilized effectively unless it is complemented by an adequate parking structure. Also the sum of the individual value of the office building and the parking structure is likely to be less than the value of the two properties combined. This notion can be extended to an entire portfolio of real estate properties to mean that the level of complementarity among properties may increase or decrease the total value of the portfolio. [Chai, 22]

2.27 Issues in the Achievement of Fair Market Value

The achievement of the real asset value poses some contradictions for privatization and RPPM. In relation to the evaluation of real property components, there seems to be a contradictory perspective regarding the achievement of a fair market value or real asset value of the transaction (see Chapter 1). From a real property management perspective, and in some cases of privatization, the maximization of the real asset value is a desired goal. However, the highest price might not be the best price in the privatization process. Key privatization guidelines address the problem restraining the possibility of changing uses in the real property used by SOEs. Literature such as the Guidelines for Country Privatization of USAID, for example, state that "precipitous privatization can be perilous and the maximum price may not be the optimum price."³ Therefore, it states that raising cash through divestiture should not normally be a priority objective in a program of privatization. The argument follows that "Where real estate constitutes an important portion of the assets of an enterprise, land speculators tend to be separated from the "legitimate business builder" [AID, 26]. It is therefore more important to have a "right buyer" that get the right price. This by leaving the land in the hands of the Government, and providing the state enterprise with a long-term lease when it has a genuine commitment to expand the business with additional investment, new technology, new markets and new management skills. The guidelines then suggest obtaining a commitment to maintain a facility in its present location and to use prohibitions against dismantling and selling facilities for use elsewhere.

These guidelines might be applicable in some cases; however the aforementioned prohibitions may prevent real property from achieving its highest and best use and its real asset value since:

a. The guidelines represent a bias against considering alternative real property uses or conversions in SOE's. The

existing SOE's function could be relocated to different facilities and the existing real property left for another use. Real estate is in most cases the most valuable asset SOEs have.

b. The guidelines bias the market forces, which should be the ones to identify the best and highest use for a particular property or enterprise, without intervention from the state.

c. The guidelines use a narrow connotation of land speculators which might bias a government's perception towards possible bidders and solutions. Real estate developers have made a positive impact in many places by identifying and putting real property to their highest and best use, different in many cases from the ones they were created for. For example, the first attempt in Moscow to privatize real estate was made in the form of an auction of four buildings. Commenting the results of this auction, a high-ranking Russian authority commented that despite the fact that the assets were sold, it was a real shame that they were bought by the non-productive sector, meaning a bank. The buyer, on the other hand, a new bank which was attempting to buy only one building for its administrative offices, ended up investing in three out of the four buildings. These buildings are now being renovated. (Other examples which can illustrate this position are addressed in the case studies in chapter 4).

d. If an enterprise is considered a candidate for privatization but the government is considering stipulating conditions for its sale such as putting limitations on disassembling an enterprise. These arguments might make sense from the standpoint of assuring that sources of employment, for example, are maintained by keeping the enterprises working. However from a real property management standpoint this scheme hinders the real property resources achieving their highest and best use. This might prove negative in the context of achieving best use of the country resources.

2.3 A PROPOSAL FOR GUIDELINES FOR PRIVATIZATION.

This section proposes guidelines for a privatization approach that takes into consideration both the basic privatization considerations described in chapter 1 and the real property management practices examined in Chapter 2. These guidelines aim at evaluating real property at the strategic and the tactical level.

These guidelines are by no means an exclusive alternative, but a compendium of steps which leave areas open for future expansion in other types of elements could be aggregated as other real property considerations are taken into account or as more research is done in the field of real property asset management.

STEP 1 Review the need for the privatization program.

This step aims at establishing the scale and the nature of government privatization/divestiture needs; checking a number of key factors that set the rationale for its proposed privatization scheme; and identifying the pragmatic, political, and operative reasons that show the need for a complementary concept to current privatization/divestiture programs. This step should take into account the principles drawn in Chapter 1.

STEP 2 The definition of objectives.

The specific goals and objectives that a government establishes for its involvement in **privatization** have important, if not crucial, implications for the selection of privatization methods. In the case of this particular work the basic criteria to be evaluated refers to the achievement of the real asset value and the highest and best use. This criteria is important for a privatization scheme that takes into account real property management practices. For the definition of strategies (which is the step 6 of this methodology) the definition of objectives is certainly important.

All objective definitions must reconcile with technical

studies. In order to consider real property market value and achieve highest and best use the privatization program must consider additional criteria besides the SOEs influence on the fiscal deficit or the feasibility of the SOEs' activities being executed by the private enterprise. Additional criteria for the identification of potential candidates is following: a) the tradeoff of value in exchange vs value in use; b) the tradeoff of useful-life vs economic-life; c) the evaluation of the highest and best use vs current use; and d) the consideration to the opportunity cost by means of the cost of subsidies and foregone rents. Then, the analysis should follow:

- a. Does the enterprise's real property have more potential for alternative use than for ongoing use?
- b. Is it feasible to relocate the function and change the real property components to a higher and best use?

If the answers are positive, then a conversion process should be initiated. This is important since a prompt decision on the method would shorten the evaluation process. One of the worst problems of the privatization process is the pressure for promptness and the lack of personnel adequate to this end.

STEP 3 The planning and management process.

This step should check the privatization process plan and management. It should check into the first privatization candidates in order to evaluate if they are achieving successful implementation.

STEP 4 The elimination of distortions.

The appraisal of the privatization program should identify those distortions that prevent the SOEs fending for themselves. This must be achieved to clarify the SOEs true situation. Distortions might be checked by means of the following: a) the lack of consideration to opportunity cost; b) the use of space subsidies; c) the lack of consideration to the value in use vs value in exchange tradeoff; and d) the need for new investments

for physical rehabilitation vs the potential for alternative uses.

STEP 5 SOEs' Real Property Evaluation

Potential candidates' real property must be evaluated as follows:

a) Valuation of the property. This must be done according to the country's valuation laws, the principles proposed in Chapter 1, section 2.3 and appendix D.

b) Evaluation of alternative uses that the property could have.

c) Determination of possibilities for relocation. Relocation must be considered: a) if the economic life of the real property components of an enterprise has surpassed its useful life; b) if an alternative use is suggested for the existing buildings and land; and c) if the use-value is less than the exchange value.

e) Executing an area analysis in which the real property occupied by GOES institutions/SOE's in a determined area are identified, checking for criteria which might be of interest for evaluating alternative uses to real property.

d) Execution of a post-occupancy evaluation (see appendix E) in order to determine the facilities adjustment to the institution necessities and whether the space is used efficiently.

Once these factors have been considered, most governments aim at identifying key enterprises which need rehabilitation and are likely to remain in the public sector for some time, or that are non-core and should be begin to fend for themselves.

STEP 6 Determine Privatization Method.

Given a single candidate or a number of them, the objectives and criteria defined, and the evaluation of this candidate/candidates, a selection among different strategies could be made to determine the best means of action.

Privatization methods proposed in Chapter 1 that consider the real property asset management practices suggested in Chapter 2 include: a) to dispose real estate as is; b) to do nothing and continue operating the institution/SOE in the real property, with improvements; c) to dispose the real estate as a whole; d) to dispose the real estate by parts; d) to undertake a joint venture along with a real property developer; g) to give a long-term lease; h) to keep for a period of time and then sell.

Besides the divestment/privatization options proposed, other additional management options that might maximize real asset value should be considered as well, such as: a) Relocation of public entities/SOE's whose real property offer potential for a higher and best use; b) market or property modifications; c) use intensification; d) real estate conversion; e) a mixed combination of alternatives.

The determination of methods depends also on the pressures of the environment. If the objective is to generate revenues to the State, and the State is in desperate need of funds, methods such as sale could be preferable to a more evenly distributed income coming from a long-term lease.

When the objective is to maximize potential income from divestment while avoiding a negative impact on future space needs. The criteria, in this case, could evaluate mechanisms that would permit the transference of the real property for a limited amount of time, such as leasing or joint ventures. Therefore, the government might reexamine its need for the property in the future and might maximize the potential income distributed in a long span of time.

STEP 7 The privatization program institutional framework.

This step must revise the current institutional structure of the privatization program to check for inconsistencies such as: a) lack of clearly defined initiatives; b) Lack of centralized authority; c) pressures on the different

initiatives; d) problems among different privatization actions and/or initiatives.

STEP 8 Real property inventory and management structure

As mentioned in section 2.24, a key issue to achieve a real property real asset value is the knowledge of current holdings. This would require the tracking the existence and accuracy of the current inventories and the current real property management structure. Does the real property inventory and real property management structure support the privatization program?

SUMMARY

This thesis, for methodological purposes, limited its discussion to one issue: the consideration of real asset value and highest and best use. The achievement of the real asset value and of the highest and best use of the real property occupied by public enterprises/entities is an important concern for privatization analysis, regardless of the fact that the purpose of a program or particular transaction may not be the generation of revenues. The chapter proposed some real asset management practices by which current privatization practice could be improved.

As observed above, in privatization with an asset management perspective, there are real property considerations besides valuation concerns which are important for the identification and evaluation of privatization candidates: a) the evaluation of the economic life and useful life tradeoff; b) the identification of potential candidates based on their potential for a higher and better use than the current use; and c) the evaluation of the value in use and value in exchange tradeoff.

NOTES OF THE CHAPTER.

1 As Lachmann [1978a : 3] argues:
Each capital good is, at every moment, devoted to what in the circumstances appears to its owner to be its "best" i.e its most profitable use, the word best indicates a position on a scale of alternative possibilities. Changing circumstances will change that position [...] Hence, we cannot be surprised to find that at each moment some durable capital goods are not been used for the purpose they were originally designed. [...] In each case the change in use means that the original plan in which the capital good was intended to play its part has gone astray. In most of the arguments about capital encountered today these facts and their implications, many of them crucial to a clear understanding of the nature of economic progress, are almost completely ignored. [Bon, 1988 : 26]

2 Real property has a life cycle. Real property has a life cycle which starts and ends with a vacant lot, the so-called unimproved land. Land is truly a non-depletable resource its value may appreciate, whereas most buildings wear out in a period of time and might depreciate. Buildings have many parallel lives: physical, economic, and technological. Many buildings can become economically obsolete when they cannot accommodate to the changing objectives and needs of complex organizations or are in the wrong location. The forces of change that bring about obsolescence can be related to changing aspirations or objectives of those organizations. Land and buildings should be analyzed separately to include opportunities of replacing just the building rather than replacing both the building and the land [Chai, 5].

3 Raising immediate cash through the sale of assets should not normally be a priority objective in a program of privatization, though it is critical that new owners have a meaningful financial stake in the success of a privatized firm. Some of the above variables can then be factored into the valuation study, with quantified estimates of what each warranty or concession might be worth, as backstop information for use in negotiating the final terms of sale.[AID 30].

CHAPTER 3 THE GOVERNMENT OF EL SALVADOR (GOES)

PRIVATIZATION PROCESS AND REAL PROPERTY INVENTORY.

This chapter examines the process of privatization of the GOES within the redefinition of its role in the economy. It tests the existence of technical and political barriers to an approach that takes into account sound asset management practices.

The chapter contents are the following: first, it examines the basic issues in the adjustment program of the GOES; second, it introduces the GOES privatization of SOEs process; third, it introduces the divestiture process that has as a purpose generating revenues to the GOES; fourth, it introduces the El Salvador Pais de Propietarios (PESPP) El Salvador country of proprietorship, program; fifth it introduces the GOES RPP; and sixth, it analyzes opportunity cost and subsidies in the RPP.

3.1 BASIC ISSUES IN THE ADJUSTMENT PROGRAM OF THE GOVERNMENT OF EL SALVADOR (GOES).

A deep structural change is now occurring in El Salvador within the public sector. This change comes as result of a move towards a market economy and public sector reduction in a drastic contrast to the expansionist and interventionist role in the economy assumed by the former government ¹. The GOES has initiated a redefinition which includes a Structural Adjustment Program (PAE) which "consists in adapting the level of expenses in the country to the level of income [FUSADES, April/1990: 2]. The following are the policies of the new PAE:

A) Redefinition of the state's role in the economy. According to the 1989-1994 Social and Economic Plan of the PAE, the government's global economic strategy consists of four basic principles: a) private property as a necessary condition for production; b) free market to insure the optimal deployment of resources; c) free competition to guarantee the functioning of the market; and d) the State as a participant in the economy limited to those functions which are its concern and/or to those

tasks that cannot be developed by the private sector and that are socially desirable. The state should not compete in productive functions that concern the private sector; moreover, it should not monopolize these activities [CENITEC, 2].

B) Full and efficient usage of the country's resources. There is an urgent need to improve the efficiency of the use of resources in order to achieve a higher rate of return.

C) Reduction of the 1989 fiscal deficit of 1500 million colones, (4.5 % Gross National Product (GNP)) characterized by excessive public expenses designated for operational purposes (80% for public salaries). In 1989 financial cuts in important social sectors such as education, health and housing, as well as in infrastructure building and maintenance were enormous [Wisecarver,-]. According to Wisecarver, four of the twenty autonomous institutions - the National University, the municipal system, the hospitals, and ISTA (Instituto Salvadoreño de Reforma Agraria) - have represented the major part of the total GOES deficit.

D) The reduction of the influence of the state is due to the redefinition of its role in the economy and to the failure of the previous government's plans. This implies radical contraction of labor² and, since 1991, of land owned by the State.

The GOES Structural adjustment includes two major programs - the Economic Development Plan and the Social Development Plan. Both involve privatization and divestiture of government assets. The programs are as follows:

1. The Economic Development Program: a) The process of privatization 1989-1991, b) The divestiture of government real property.

2. The Social Development Initiative: The "El Salvador Pais de Propietarios Initiative" (El Salvador Country of Proprietorship).

3.2 THE PRIVATIZATION PROCESS.

Privatization is a key issue in the GOES structural adjustment program (PAE) which seeks to promote economic development by reducing the government's major fiscal deficit, reducing the public-sector size, and transferring functions that the state has managed inefficiently. The scope of this program aims at privatizing any government function that could be supported outside the public sector, given the GOES fiscal limitations.

The following analysis of the privatization program of the GOES follows these steps: first, it highlights the major components and actions of this program from 1989 to 1991; second, it describes the major actions ahead; third, the problems found by this program; fourth, it examines this program in light of the proposition presented in Chapter 1. The privatization program from 1989 to 1991 has focused on the following actions:

a. The denationalization of public functions such as the export marketing boards, including Instituto Nacional del Cafe (INCAFE), Instituto Nacional del Azucar (INAZUCAR), and the financial sector (nationalized in 1982).

b. The closing, leasing, or contracting out of government services or functions that can be provided by the private sector, such as the transference of educational services and administration such as the Instituto Tecnologico Centroamericano to Fundacion Educacional para el Desarrollo Economico (FEPADE).

c. Complete or partial divestiture or liquidation of state owned enterprises SOE's, or entities which have the most impact on the fiscal deficit, for example, the definite closing of the Instituto Nacional de Abastecimientos (IRA), paraestatal institution in charge of regulating grains and milk prices.

d. The closing of government services which could be provided by the private sector. The liquidation of the Instituto Nacional de Vivienda Urbana (IVU), followed by restructuring to integrate the program of this institution to

the housing plan 1989-1994.

The privatization of SOEs has not had as its focus real property; however real property is affected. Some candidates for privatization which are the subject of analysis of this thesis (see appendix 3 for further information) are the following: a) The closing of the Instituto Salvadoreño de Investigaciones del Café (ISIC); b) The Hotel Presidente; c) The Feria Internacional De El Salvador (FIES); and d) the Lechuza tube factory.

The privatization program has had two initiatives. First, a loose decentralized decision-making process has prevailed in the privatization process from 1989 to 1991. The effort existed under institutions/committees ranging from the President and the Consejo de Ministros to the different institutions involved such as ministries. Second, a centralized privatization decision-making process by means of a privatization commission was established in May 1991. [La Prensa Grafica, 4/8/91, 2]. The commission has the responsibility to make the privatization program succeed and to identify and analyze potential candidates.

3.3 THE DIVESTITURE PROCESS.

The GOES divestiture program aims at raising revenues by means of selling government real property which is vacant or empty. The 1990 budget calls for an extraordinary disposition of twenty million colones (eight colones = one U.S. dollar) of surplus real property assets. This exceptional measure was taken because of the extraordinary fiscal crisis that resulted from the decline of income tax; which in turn was due to the fall in world coffee prices. This program includes:

- a. Vacant downtown land previously occupied by government facilities destroyed by the 1986 earthquake.
- b. Real property belonging to institutions such as Instituto De Vivienda Urbana (IVU) and Fondo Social para La Vivienda. These institutions have offered their land on the open

market by means of newspaper advertisements.

- c. The IVU land and/or building portfolio, worth 1000 million colones. This disposal aims at investing the revenues from a potential sale in the housing program either by:
 - . Sale of land and/or buildings to private investors. The old IVU buildings worth 21000000 colones, for example.
 - . Transference of land destined for housing for the PESPP program (see next section). This program is executed jointly with IVU and Corporacion Salvadorena de Inversiones (CORSAIN).
 - . Housing and apartment units sale of property rights to their current occupants.
- d. The divestiture of assets of institutions being privatized. The INAZUCAR and INCAFE, for example, includes facilities for uses such as: administration, coffee grain processing, and sugar cane processing facilities (ingenios). A complete analysis of the results of these initiatives is beyond the scope of this document.

For the GOES, the divestiture of real property assets is neither considered part of the current privatization effort, nor as part of the restructuring/adjustment program, nor as an option in the five-year GOES plan.

The emphasis of the GOES privatization program on the generation of income has been relatively small. What are the reasons why the state should give more emphasis to the generation of revenues? (see section 5.1).

3.4 THE EL SALVADOR PAIS DE PROPIETARIOS (PESPP) PROCESS.

The housing program is a major component of the Plan de Desarrollo Social. This initiative aims at reducing the effects of the PAE in approximately 65% of the population living in extreme poverty ³. A subset of this program is the "El Salvador Pais de Propietarios" (PESPP) program--El Salvador Land of Proprietorship ⁴. The PESPP aims at utilizing the dynamics of

private property in low-income sectors, by means of the following measures: expedite the legalization--by selling land and tenure to low-income communities living on government land; enable access to credit to people who traditionally have not had such access. The PESPP program attempts the following:

- . Gathering an inventory of publicly-owned real property, that could be used for the construction of popular housing. The inventory is known as "El Banco de Tierras".

- . Coordinating the disposal of 50% of the land owned by the State and the municipal system. This excludes forestry reserves and highway and train rights. This program will give 600,000 titles of proprietorship to low-income families.

- . Obtaining revenues through the disposal of publicly held land designated for financing the investment on land for other low income housing projects.

The PESSP program takes place in a context of haste, provoked by political pressures, for distribution of the increasingly scarce land such as the following:

- a. The distribution of government held land to communities was one prerequisite to end the war, now in its 11th year of conflict. This was a compromise made on October 1991 between the GOES and FMLN at the U.N. Peace Talks.

- b. Recent occupation of land by the homeless and by squatters has provoked an issue of great concern to the Salvadorean community. Most properties occupied have been government owned.

- c. A real property inventory was key to these pressures, as discussed in section --. However, it is important to consider why there was not such pressure on the State until recently.

3.5 ISSUES IN THE REAL PROPERTY PORTFOLIO.

The GOES PAE policies outlined above call for change in the vast real estate portfolio concentrated in the hands of GOES institutions and enterprises. An inventory started in 1989 by

Vice Ministerio de Vivienda (VMV) (Vice Ministry of Housing) reports on table 3.1 partial data of the real property inventory of GOES institutions.

3.51 The Inventory size.

The partial amount of land reported is 948,659,375 square varas (V^2) (one vara is equivalent to 0.83 meters), equivalent to 769,078,150 square meters (m^2) [186,515 acres] or 769 square kilometers (Km^2). Considering that the size of the country is 20,000 km^2 , almost four percent of the territory is owned by the government. Most of this real property inventory is vacant. The GOES is by far the largest landowner of single ownership in a country where constitutionally the area for a property cannot exceed 445 HA. The GOES, as the major owner of urban and rural land, maintains most of the "free" land for development of vacant or under-utilized properties. Therefore, the GOES creates land scarcity, uncontrolled growth of cities and subutilization of infrastructure.

The amount of land in this inventory might appear small in relation to the country size if one considers countries such as the US, where the government owns 33% of the land. However, it is a large proportion in a country so small and overpopulated (300 inhabitants per Km^2 or 1.23 inhabitants per acre). Scarcity of land is a critical issue in this country where a majority of the population are not land owners. There have been various government interventions ⁵ to redistribute private land but no effort has been directed toward the extensive publicly-owned land inventory that is idle.

Added to this consideration, there has been a dramatical decrease in the amount of urban and rural vacant land available for development that could be sold on the open market. This decrease on land parallels the increasing pressures for the distribution of the remaining land - either by squatters (see section 3.3) and/or by the development community (see section 3.2). These pressures, added to the need of GOES to get

GOES REAL PROPERTY INVENTORY

INSTITUTION	NUMBER OF PROPERTIES	AREA V2
M A G	85	24,913,353.09
MINIST.CULTURA Y COMUNIC.	90	1,021,233.17
MINIST.DE EDUCACION	850	26,316,763.27
MINIST.DE ECONOMIA	4	50,103.83
MINIST.DE HACIENDA	300	46,994,524.29
MINIST.DEL INTERIOR	150	12,660,163.19
MINIST.DE JUSTICIA	30	789,267.39
MINIST.DE LA PRESIDENCIA	1	900.33
MINIST. DE RELAC. EXTER.	3	10,911.10
MINIST. DE SALUD	200	2,125,870.13
MINIST.DE SEGU.PUB.	60	22,202,033.15
MINIST.DE TRABAJO	4	43,833.70
M O P	800	213,876,640.78
PODER EJECUTIVO	5	86,960.74
PODER JUDICIAL	1	827.78
A N D A	50	395,825.02
A N T E L	40	68,404.38
BCO.FOMENTO AGROPECUARIO	52	623,697.42
ALCALDIA USULUTAN	6	21,264.50
C E L	135	8,011,526.31
FERROCARRILES DE EL SALV.	140	6,344,713.54
FISCALIA GRAL.REPUB.	6	1,588.06
FINATA	180	22,394,594.55
FONDO SOCIAL	25	282,612.61
G O E S	300	274,960,006.54
I C R	9	236,017.95
I R A	1	20,000.00
I S S S	3	184,406.36
I S T A	35	278,441,945.62
I S T U	20	755,833.42
I V U	35	4,823,553.18
TOTAL	3620	948,659,375.40

* partial data

Source: Inventory of the Vice Ministerio de Vivienda
with data from the Direccion de Registro de la Propi-
Ministerio de justicia

TABLE 3.1

. notes to Table 2

The inventory does not include:

- . The vast property portfolio of the municipal system.
- . The total of properties are not reported.
- . Properties with unclear legal status or occupied by other institutions.
- . Land reserved for highway rights.

revenues create a hurry-to-sell atmosphere, which could in turn, deflate the real asset value.

2.52 The inventory value.

The reported value of 90,635,671 colones for the total amount of real property owned by the government is extremely low. This estimate is based in the following evidence:

. This reported amount accounts for a value of approximately 0.1 colon per square vara V^2 . This price is extremely undervalued considering that land in the countryside goes from around 7 colones per V^2 to 80 colones per V^2 . Land in the urban area of San Salvador is worth from 150 colones to 1000 colones per V^2 . Taking, as a mean, a very conservative assumption of 20 colones per V^2 at market value, the total value of the real property inventory value would be approximately 20,000,000,000 colones.

. This reported value is based on historical data that is extremely low in relation to market prices - for some properties 300 times less. A property in the inventory has a reported a value of 1 colones V^2 and a current market value of 300 colones.

. The eleven properties considered in the case study in Chapter 5, are worth more than 3.7 billion colones. This sample of properties is minuscule compared to the rest of the properties in the metropolitan area of San Salvador alone, not to mention the totality of the inventory which includes 3000 properties.

. In 1989, when the first estimates of the real estate assets of the I.V.U. showed a value of 1000 million Colones in assets, vacant land was worth 500 million colones. Mauricio Stubig, Minister of Public Works, commented on this inventory:

"At the moment, the real property assets of each government institution are being audited, we have realized that there are properties that have an underutilized capacity and properties that we never even thought were part of the patrimony of each institution. In the case of IVU, for example, only with these assets could we reactivate this institution in three years."
[Stubig]

2.53 The Inventory type.

Exhibit 3A highlights different types of GOES's real property. Given the absence of a real property inventory or accurate data about size, use, and level of utilization, this table is based on direct observation and research done at various institutions.

Exhibit 3A	GOES REAL PROPERTY PORTFOLIO
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- a. Vacant Land. This category includes vacant or underutilized urban or rural raw land guarded on the perception that the State needs to hold land for the day, when it may be required for the Government's institutions or facilities to expand. This category includes land such as:
 - . Land reserved for future government expansion.
 - . Land reserved parks or conservation areas.
 - . Highway, train and air rights.
 - . Leased land
- b. Land occupied by squatters.
 - . Land reserved for highway or trains rights.
 - . Land reserved for future expansion overtaken .
- c. Buildings and land for governmnet entities.
 - . Government headquarters,
 - . administrative facilities,
 - . support facilities, such as gas stations, mechanical workshops, parking lots, cafeterias, electrical services, cleaning service.
- d. Buildings and land for non-administrative facilities. Some types of properties in the GOES real estate portfolio are to a large extent, dictated by the character of the Government institutions primary activities).
- d1. Transportation system facilities.
 - . Airports, and related facilities
 - . Ports, and related facilities
 - . Highways related facilities and highway rigths.
 - . Railroads, related facilities, and railroad rigths

- d2. Financial Services facilities:
 - . bank headquarters and Branch offices.
 - . Bank holdings such as office; commercial, housing and apartment space takeover to third parties.
- d3. Service Facilities:
 - . Telecommunications, ANTEL
 - . Hydroelectric plants CEL.
- d4. Industrial property: These are properties which include facilities with manufacturing or warehouse purposes. Examples of this type of property in El Salvador are:
 - . Free Trade Industrial Zones (Zonas francas).
 - . Plants for sugar production (Ingenios).
 - . Coffee production plants (Beneficios).
 - . A plant for the elaboration of Gasohol.
 - . Grain Silos for IRA.
- d7. Facilities for services.
 - . Hotels. Hotel Presidente, 245 rooms. Hotel de Montana.
 - . National theaters. (Circuito de teatros Nacionales). Cinemas, around 30 countrywide.
 - . Stadiums, Parque de Pelota, Estadio Nacional.
 - . International Fair, and sport facilities countrywide
 - . Municipal market system.

Exhibit 3A

SUMMARY

The GOES privatization program involve different types of initiatives. There are three basic objectives in the GOES privatization initiatives: a) to eliminate functions that are a drain to the fiscal deficit or could be executed by the private sector; b) to liberalize assets; c) to dispose of real assets so as to provide an alternative source of income for the government, getting revenues as result of divestiture. In this cases the consideration of real asset value is especially important; and d) to provide land to squatters.

NOTES OF THE CHAPTER.

1 The past Christian Democrat government had an excessive expansion in the 80's and assumed an interventionist role in the productive sector of the economy. [Plan de desarrollo, 37]. Wisecarver in his book about the public sector of El Salvador in 1989 analyzed that through all its ingerence in the national economy, the past government had achieved an economic system that could just be compared with the one of a statized country or in some sectors a socialized country. The quality of spending /.../ together with the nature of its interventions and regulations, (not to mention the attitudes and perspectives) are the factors which weight more against the private sector in the country and have destimulated economic and social development. This threat must be overcome to reactivate the salvadorean economy". [Wisecarver,4].

2 There is a trend to reduce the government personnel, between 1984 and 1989, Employment in the public sector fell from 118,949 jobs to 111,418 [Wisecarver:15].

3 The definition of extreme poverty is referred to those sectors of the general population whose income is lower or equal to the cost of the "canasta basica" of food. In 1980 according to CEPAL, half of the salvadorean population was under extreme poverty conditions and up to 42.4% of the rest it almost did not satisfy its food needs, housing, educational and otehrs. MIPLAN data describe that in 1989 55% of the population was in conditions of extreme poverty and in 1990 the percentage reached 63% [FUNDABAL, 2]

4 In the first months of 1991, the GOES anounced the creation of the PESPP under the Instituto Libertad y Progreso (ILP), this is a program that is within the PAE compensatory program. The PESPP is a functional measure, aimed at modernizing the government aparatus, that sticks to the liberal conception of property that considers this one an absolute right. It pretends to create quick mechanisms that make easier the legalization of land. The beneficiaries are people that have been occupying land that for legal reasons have not been able to legalize.

5 In 1976 a project of agrarian reform lasted for three months and failed. In 1981 another agrarian reform took away from its original owners 300,000 manzanas of land for agricultural purposes, 12% of the agricultural land available in the country. After this an intense debate followed trying to find the maximum amount a person could have and it was defined at about 560 manzanas or 445 HA as stated above.

CHAPTER 4.

CASE STUDIES.

This chapter evaluates case studies of the current GOES privatization approach introduced in section 3.1. These case studies are evaluated in contrast to the theoretical framework proposed in Chapter 2.

This chapter poses the following question: Does the present privatization evaluation approach, at both strategic and tactical levels, consider the real asset value and the potential for the highest and best use of the real property occupied by entities/SOE's. It presents two case studies. The first analyzes an ongoing privatization candidate. The second examines three SOE candidates for privatization and other GOES entities in their surroundings, demonstrating the rationale for a joint evaluation of privatization candidates.

CASE STUDY 1: THE INSTITUTO SALVADOREÑO DE INVESTIGACIONES DEL CAFE (ISIC)

Background.

The Instituto Salvadoreño De Investigaciones del Cafe (ISIC) was a coffee research institution which serviced the coffee producing community in El Salvador. The ISIC facilities included 10.9 HA of land, 3000 m² of administrative buildings, laboratories, and experimental coffee plantations. These facilities were located in a prime development area of Santa Tecla. The ISIC was established in 1950, on a coffee plantation. Now, after 30 years this non-intensive use facility is surrounded by new residential development. The real property has a market value estimated at 25 million colones by Direccion General de Presupuesto (DGP) (General Budget Direcction). The facilities are in a period of high obsolescence and high deferred maintenance.

Current privatization situation.

In 1989 the GOES identified the ISIC as a candidate for

privatization. This decision was based on the rationale that the government was not going to execute activities that could be run by the private sector. A key argument in taking such a stance was that such an important institution (considering the importance of coffee in El Salvador) should be kept apart from political influences of any government. Based on the agreement between the government and some coffee production sectors, the institution was to be privatized and its function given to PROCAFE which would represent the interests of all the coffee producers.

A research study, Tropical Research, financed by USAID developed a set of guidelines with steps to be implemented. These guidelines stated that PROCAFE, the new entity, would receive the existing land, installations and equipment. The research concluded the land should be sold to the new research institution. Therefore the government, in an arrangement with USAID was going to make a donation in land, facilities and equipment totalling 1.8 million dollars (market value of those facilities lay mostly in land accounting for 3.2 million dollars). This transaction did not preclude the new institution from later selling the land and relocating.

A second research group was consulted in order to value the ISIC's fixed assets and to study possible legal mechanisms for the transference of the assets to the new entity. However this property was mentioned in a paper [FUSADES, July 1990] as having potential for alternative uses, and for this reason the author was called upon as consultant for this second research project.

The second research group proposed an alternative scheme. The new research determined that the current location of ISIC was not viable, for the following reasons:

- a. From the legal standpoint, the property was owned by the GOES, not the ISIC as thought before. Therefore there was no obligation to donate any land or installations to PROCAFE.

- b. From the technical standpoint, research installations and plantations should be able to reproduce the conditions of

coffee plantations in the countryside. The urban setting would make it difficult such conditions. The setting would incur noise and smog, which would even affect the measurements of the laboratory equipment.

c. From the operational standpoint, a highway that had been scheduled to be built in the north side of the plot would separate the laboratories from the coffee research plantations, which would make the research less feasible.

d. From an economic standpoint, the land was being undervalued. A later valuation estimated the value at 25 million colones. At such value, the land was too expensive having in mind its use for coffee plantations. Tropical Research had not considered the possibility of giving the property an alternative use and relocating the existing facilities. A highest and best use analysis showed potential for residential developments. The inclusion of a new highway passing through the land would increase its real asset value.

The recommendation suggested an interim lease and relocation of the new entity PROCAFE in about four or five years. This recommendation raises two issues:

a. The new institution leases the land for a limited amount of time. After four or five years the new institution relocates. This would give sufficient time for experimental coffee trees to start growing, meanwhile not losing the existing research. The cost of this relocation should be part of the new institution's concerns.

b. The new uses for the land and buildings have not yet been determined yet. Such uses could range from creating a park and mixed recreational and residential developments, to the construction of the Agriculture Ministry headquarters.

The fact that the Tropical Research study results were adopted, reflected in the first GOES policy to not consider the option of relocation. This resulted in a costly mistake, since the GOES compromised by donating 1.98 million dollars -- the

assumed value of the installations and land which were thought to belong to ISIC. Under different conclusions the money for the new entity could likely have come from a the donation agency, USAID. However since this compromise was taken, USAID found that it hard to justify spending more money on the project. Hence the GOES had to find the money from its own sources. The new research institute has to get the funds from sources excluding the GOES or USAID.

Regardless of the costs, the real property will most likely achieve a higher and best use. The real asset value of the land was considered and it was estimated at almost 3.2 million dollars, which would have been lost if the land had been considered agricultural land subsidized for the new private research institution.

This case has demonstrated a scenario where the property occupied by an SOE was located in a prime development area, with potential for a higher and better use over the current one. The Tropical Research scheme, based in the current approach to privatization, did not identify these characteristics, resulting in the real asset value not being recognized.

In the second approach the different characteristics of the property were analyzed, resulting in the feasibility of relocating the institution and using the current facilities in five years either for sale or for other government uses.

CASE STUDY 2. SAN BENITO AREA GOES SOE'S/ENTITIES REAL PROPERTY PORTFOLIO

This case examines three SOEs which have been identified by the GOES as potential candidates for privatization mentioned in section 3.2: the FIES, the Lechuza tube factory, and the Presidente Hotel.

The three enterprises share in common the following facts: that they have more potential as alternative real property uses than their ongoing uses; they could be privatized as active enterprises and according to their real property value; they

represent little or no social impact if privatized or divested; they are both economically and physically obsolete; and they are at adjacent locations in the same prime development area of the city. The latter characteristic allows the possibility of analyzing the real property of these SOEs jointly and/or in conjunction with other government properties in the area. The common location is a common phenomenon in government institutions. In these locations the GOES has developed SOE's/entities unrelated in their products. The adjacency of these properties, however, makes the evaluation of their joint real property characteristics essential for the achievement of the real asset value. The government assembles a big piece of land, and in time, surrounding development add to its value.

The fact that this proposed type of evaluation is not considered in the GOES current privatization analysis is based on three facts: there is not an overall vision in the analysis of SOEs; the real asset value is not considered; and the analysis has been done basically in isolation as a result of the current loose privatization scheme (see section 5.7).

All these enterprises currently share the similar financial losses (or breakeven) versus a high opportunity cost of the real estate they occupy.

The latter privatization candidates call for the attention of this study since they involve enterprises of particular interest from a real property management perspective for the following reasons: a) the economic life of their real estate has been surpassed; b) the current use is not the highest and best use; c) the market value has increased markedly; and the use value is low and prospects of exchange are good.

The case study includes the following: it first introduces the area and its changing dynamics; second, it studies each individual SOE and the current efforts towards its privatization; third, it analyzes their real property characteristics and the argument for change of use; fourth, it examines the foregone opportunities if these candidates are

evaluated in isolation and as ongoing enterprises as it would occur under the GOES current privatization scheme. It then examines advantages, if any, of a joint analysis of these SOEs based on their adjacent real estate.

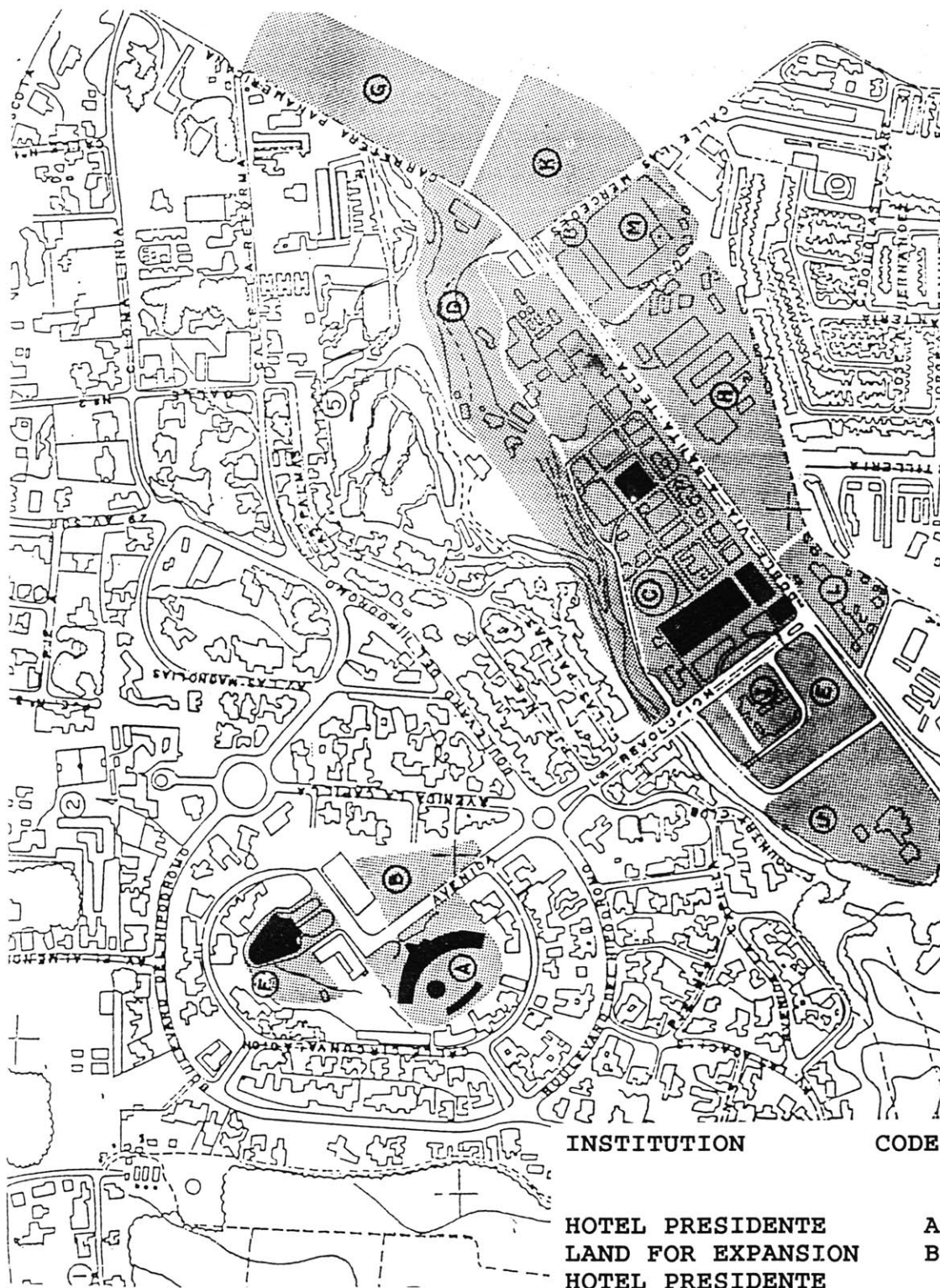
4.21 Description of the San Benito Area:

The San Benito area is located to the southwest of the San Salvador Metropolitan Area (AMSS) (see map 1) and it is the prime development area in the city. It has one of the best infrastructures in the AMSS. For a description of the area see Appendix. The sources for this information have been Dirección de Catastro Fiscal for prices of land; Instituto Geográfico Nacional and Oficina de Planificación del Area Metropolitana, for maps, or on site information when feasible.

The San Benito infrastructure was designed in the 50's to be the Government Center of the AMSS. However, the proposed location of the Government Center was switched to the Finca Modelo where it currently stands. This arrangement gave rise to the San Benito residential area. However, the infrastructure for the Government Center had already been built, and included wide boulevards, and monuments. It became an area of residential houses and monuments, both of beautiful architecture.

The GOES kept at that time, an extensive part of the area, and bought at very low price the golf courses of the El Salvador Country Club with more than 60 HA. Given the suburban characteristics of the area at that time, the government gave these lots to non-intensive-space-use institutions mentioned in the cases studies and others mentioned in the Appendix 4.1.

The land and facilities used for institutional purposes have now acquired a great potential for other uses. Given the change of the area in the 80's most of its residential use became to commercial/office/apartment space. This intensified use of space and new developments in the area engulfed the



MAP 1

INSTITUTION	CODE
HOTEL PRESIDENTE	A
LAND FOR EXPANSION	B
HOTEL PRESIDENTE	C
FERIA INTERNACIONAL	D
LA LECHUZA	D

public sector facilities, creating non-intensive-use pockets. This creates incompatibility with the trend for growth in the area. Some government institutions disrupt the normal growth and behavior of the surrounding areas. For example, there are various institutions that are no longer compatible with the area, such as military installations (see page Appendix 4.1).

The increasing demand for commercial and office space in the area has provoked the following:

a. Space intensification and changing uses of the existing large residences in the area. The construction area ranges from 400M to 2000 M² and the land plots are of 2000 M² or higher. There are residences in the area abandoned by owners who fled the country because of the war.

b. In the last two years as old space became less available, thousands of square meters of space were built and projected in the area. New buildings such as the Zona Rosa (the largest concentration of restaurants, cafes, and clubs in the AMSS), Torre Democracia, three new shopping malls, banks, and corporate headquarters, are examples of such projects.

c. Increasing land values. The land in this area is now one of the most valuable of the country. Land prices range from 450 to 1000 colones per square meter (1 vara is 0.8301 meters) or 50 to a 130 dollars per square meter (according to data in the Banco Hipotecario, Direccion de Catastro Fiscal, and real estate sources). According to the Direccion de Catastro Fiscal, land prices in the area have grown in value from 80 to 700 Colones in ten years.

Among the forces that provoked this increasing demand in the area and which also changed the patterns of development of the AMSS were:

a. The civil war which started in 1979, provoked a major move of institutions/corporations to the area. This area has been defined as "most secure" by foreign entities, embassies, and corporate headquarters. The already high standard of living in the area has increased, creating a demand for

commercial/office space.

b. Residential influx in the city because of migration. and the growth of population in the surrounding areas. This was originated by the development of the area of approximately five kilometers between San Salvador and Nueva San Salvador. Nueva San Salvador itself has grown from 100,000 to 400,000 inhabitants in six years. This area, known as Ciudad Merliot, is a middle class and working class neighborhood with existing industrial/service facilities. There are no official figures on this growth because due to the lack of a census.

c. The 1986 earthquake, destroyed or damaged a major portion of the public-sector infrastructure provoking a move of the banks' headquarters and public and private offices, from downtown to San Benito.

4.22 Hotel Presidente Complex and land for expansion.

The Presidente Hotel was created by the government in 1976 based on the expectation of expanding tourism. The management of this state hotel was leased to the Hyatt Regency. Given the drop in tourism at the start of the civil war, in 1980 Hyatt stopped operating the hotel. The hotel facilities were passed on to CORSAIN, the Government entity in charge of the management and now in charge of the prospects of privatization.

The Hotel was the government's first candidate for privatization. There have been attempts to privatize the Hotel since 1985 with no substantial offers, according to the CORSAIN management. An offer made in 1989 for 35 million colones was rejected because it was considered too low. The real estate profile and criteria for evaluation are presented in Exhibit 4.1.

Current privatization situation:

The decision-making process regarding this hotel has always been based on the expectation that if tourism expands in the country this major hotel will be necessary. Therefore the GOES should not sell it for another use. This has led to lost

Hotel Presidente profile.

- . Land size. 25,692 M² for the lot occupied by the Hotel complex and 20,701 M² for a lot of adjacent reserve land.
- . Facilities. The facilities built in 1976 occupy 16,300 M² and a construction value of 2,500 colones per square meter. The facilities are well built; high deferred maintenance.
- . Market values. Because of the area characteristics, the price goes from around 500 to 700 Colones per V². Being the hotel and facilities valued in 1989 at 54,000,000 colones based in replacement cost. Estimated market value of 70 million colones [1989 valuation].
- . Under-utilization. The hotel maintains a 35% occupancy, remaining 65% vacant most of the year [1989].
- . Financial situation. The state has carried losses operating this hotel for almost ten years. Such losses have resulted from a high vacancy rate, under-utilization, and obsolescence. The government renovated and the hotel to make it more attractive, but the investment has not proven effective. This reflects the lack of consideration to the evaluation of the investment costs vis-a-vis the potential revenues in public investment.
- . Use-value/exchange-value tradeoff. This hotel has a use value for the government of 685 colones based on NPV/m², which contrasts with the exchange value of 2,300 colones. The Hotel had an expected life of 40 years but has gone into deferred replacement since there are almost no revenues.

EXHIBIT 4.1

opportunities. In 1989 there was high vacancy rate at the hotel and the increase of demand in the area for apartment and office space was high (a consequence of the 1986 earthquake and the continuation of the war). At that moment a research study estimated that the hotel could be partially converted to another use, remodeling and using its second floor for office space at a very low cost. However, CORSAIN did not take advantage of the opportunity. Another alternative could have been to convert the hotel to office space and condos, with a club and a convention center in the common facilities. This follows the

rationale that at that particular moment it was better to divest the property to a potential buyer who had other objective than the hotel in mind. However there is a bias towards keeping the ongoing uses, which has resulted in the continuation of losses and the lack of consideration to the real asset value (see section 2.2 Guidelines). If the market forces were left to flow freely they would identify when a major hotel was necessary again, but in the meantime both the state and the development sector would have benefitted from an unbiased policy of privatization. The state would then have benefitted from the potential income coming from this operation and would have saved financial resources by means of credits of the nationalized bank system to build new facilities by increasing the offer of space in the area.

4.23

La Lechuza, Tube Factory.

Current privatization situation:

La Lechuza is a factory for the production of concrete tubes, owned by the Ministry of Public Works (MOP) and used by the Direccion General De Urbanismo y Arquitectura (DUA). The factory was considered by DUA as a potential candidate for privatization as an ongoing-use. However this matter has not been pursued because the factory does not report losses and the State would have to find an interested buyer that would like to invest. The Lechuza facilities are obsolete. If the price of land reflects the real asset value, then a privately operated tube factory would not be profitable here. Because of its location, the real estate has a potential for various higher and better uses. It would be worth considering the possibility of relocating the factory. The real estate profile and criteria for evaluation are presented in Exhibit 4.3

La Lechuza, profile

- . Land Size the lot is 49,719 M² (71,159 V²).
- . Land values. Because of its land characteristics, 60% of the property is a river depression, the land value is lower than the surrounding areas, being worth around 400 per m². This also given the necessary infrastructure and the land filling necessary to develop the property
- . Age. Most facilities were built in the 60's.
- . Legal status. The land is disputed between the FIES, who paid 300,000 colones for a plot worth 35 million, and DUA.
- . Use value-exchange value tradeoff. The Lechuza has a use value for the government of 6.60 colones based on NPV/m² which contrasts with the exchange value of 752 colones.
- . Degree of obsolescence. The facilities are of temporary type, with a high deferred maintenance.
- . Under-utilization. The tube factory is barely used, a plant for the elaboration of asphalt for highways is not used.
- . Relation to city growth. The Lechuza is the only place by which the FIES can directly communicate its central section and the San Benito area (see map). The facility is surrounded by housing to the north, the international Fair to the south and the Pan American Highway to the east. There is demand in the surroundings for commercial/office/apartment space.
- . Feasibility of relocation. The facilities used by the IVU could easily be relocated according to Architect Bara, President of IVU. The asphalt plant is obsolete because of the construction of another plant with higher capacity.
- . Low social impact. The relocation would only affect the staff (20 men) working in the tube factory.

EXHIBIT 4.2

4.24 La Feria Internacional De El Salvador (FIES)

The Feria Internacional de El Salvador (FIES), is an Autonomous institution that inaugurated in 1965. It operates under the Ministry of Economy. The intrinsic nature of the FIES is to rent its facilities to commercial representatives of foreign governments or to local firms. The FIES host a major export-import events the Feria Internacional de El Salvador once every two years. The real estate profile and criteria for evaluation are presented in Exhibit 4.3

The possibility for the FIES to become a privatization candidate was first publically proposed by the Minister of Economy in mid 1990 in a TV interview. The minister proposed an ongoing enterprise. The FIES was also suggested by a FUSADES study to be privatized as an alternative use. The FIES falls under the redefinition of government objectives. What would happen if the FIES were privatized, and how would the consideration of the prime location of its real property and its real asset value affects the privatization evaluation?

The FIES is an SOE that occupies a large, very valuable, extremely underutilized, prime piece of real estate which has potential for a highest and best use. In order to keep the FIES operating the government must ignore the high opportunity cost of holding the facilities for current use and therefore the real asset value; the subsidies to the FIES in form of free space; and the acceptance of poor outcomes for social or financial reasons.

Feasible strategy scenarios for the FIES.

The government should consider various alternatives based on the privatization methods presented in chapter one and the criteria that could be gathered form the real asset management experience.

- . To keep the current use in which case, the GOES would not acknowledge the real asset value.
- . To intensify the use of the FIES.

Feria Internacional de El Salvador (FIES) profile.

. Land size and value. This property occupies an area of 210,000 m² (286,123 v²). The value has increased from 100 to 700 colones per m² in ten years [DCC]. Market value if facilities were sold, is estimated at 186,000,000, adding to 156,000,000 for the land and 30,000,000 for the facilities (depreciated 50%)

The parking lot of the FIES is approximately 41000 square meters, valued at approximately 600 colones per square meter, a total market value of approximately 25 million colones. The parking lot can accommodate 2000 vehicles and most of the year it is not used except for sporadic events at the FIES, or for soccer games over the weekend. This property has been and under increased pressure to change its current use, therefore there is a possibility of leaving the FIES without a parking lot. The MAG has thought of putting some of its facilities there. A project was designed there also, to relocate all the government institutions into two 32 floor towers after the destruction of the 1986 earthquake on GOES installations in government center. There is a trend to analyze this property aside from the FIES.

. Facilities size: The FIES installations have 40000 m² of constructed facilities worth approximately around 1500 colones/m². Most facilities were built between 1964 and 1976. The FIES is composed of 50 exhibition facilities and warehouses. Many facilities were built having a high churning rate in mind so they have a flexible design and non-permanent character. The buildings are one floor, except for the main pavilion which is of 10,000 square meters and has a mezzanine.

. Dynamics of change of the site. Given the rapid changing pace of commercial activity in the area (explained above) and its strategic location in the center of the physical growth of the AMSS, the FIES is a case which offers various alternatives for analysis. The current FIES facilities are located on the Pan American Highway, the main communication line in Central America. The subject site is well located in relation to other public facilities and support services. Given the pattern of market demand in the area the of FIES, the highest and best use for this lot is a mix of commercial, office and housing space.

. Legal status. The land is owned by the Ministry of Agriculture and is leased at no charge to the FIES. However, the 50 year lease which was offered in 1965 has not yet been signed. Until 1990 the high-level MAG officials neither know that the property belonged to the Ministry, nor were they aware of the status of ownership of the facilities that have been built in this area as was shown by this research. Nevertheless the perception of government officials is that the property

belongs to the FIES. This is a situation present in most SOEs of the GOES (same case as ISIC). The parking lot of the FIES, located south of the International Fair, belongs as well to the MAG but it has not been acknowledged that it is included in the unsigned lease. This presents demands by various GOES entities and developers. for changing the use of this apparently vacant real estate

The rationale to privatize for alternative uses or for assigning the real property a different use comes about because of the following factors:

- . Use value-exchange value tradeoff. The FIES has a use value for the government of 18.9 colones based on NPV/m² which contrasts with the Exchange value of 1108 colones. Some installations had an expected life of 30 years but has been going into deferred maintenance, since there are almost no revenues. Many facilities are of the warehouse type.

- . Outputs. The revenues are 300,000 colones every two years. The FIES experiences revenues one year and losses in the next.

- . Need for rehabilitation. The facilities have growing obsolescence and high deferred maintenance in addition to a physical and economic obsolescence. Last year the FIES invested 4,000,000 colones in repairing for the event.

- . The high degree of deferred replacement and the reduced output indicates that the FIES is at a declining stage in its real property cycle.

- . Subsidized Space. Both the GOES and the FIES management agree that the institution could run perfectly under the private sector. However, when presented to the current management, the consideration that if, as a private buyer the new entity should have to pay at "fair market value" for the land and facilities, this idea is questioned. The question that arises is: should the GOES subsidize the continuation of the event by means of free land and facilities, or keep a lost opportunities by ignoring the high opportunity cost of the real property. In 25 years the FIES has paid no rent for the land and it has reported little benefits income. The scenario of free-land-subsidies to the FIES is treated in section 5.4

- . Current usage. The FIES has undergone profound changes and transformations in nature and uses in 25 years due to external or political circumstances.

- . High degree of under-utilization. Under-utilization of space shows that:

- . The need for the FIES as an event is decreasing. The time span between each fair has increased from one year to a two year and the duration of the FIES from 25 days to 13 days.

In the meantime it has housed events far from the FIES initial objectives ranging from trading events (highly criticised) to cattle exhibitions.

. The under-utilization of space on the FIES makes the FIES installations attractive to other GOES institutions which are continuously pressuring to get space. The FIES facilities have been increasingly occupied temporarily or permanently by its strong neighbor the Estado Mayor, which has already definitely taken over some facilities .

- * to host extraordinary events such as: being a facility for the Consejo Central de Elecciones (central body that organizes the elections in el salvador),
- * Hosting government institutions such as the Ministerio de Hacienda and Ministerio del Interior affected by the 1986 earthquake.
- * A permanent site for the San Benito battalion 1 .

. Changes on space dynamics. The FIES management acknowledges that the FIES event will tend to disappear and that the trend is going toward more specialized events ² which implies a contraction in the need for space of the FIES. The current use yof the FIES to host artistic events and official ceremonies may end with the reconstruction of the national gymnasium (with a capacity to accommodate 15000 persons) which was where these events were held, before the 1986 earthquake.

. Externalities and Incompatibility. The FIES installations which constitute a source of disruption for the area when events take place. Approximately a million visitors go to the fair during the peak time span which last 17 days; informal commerce surrounds the FIES and traffic jams in the surrounding streets. This situation is intolerable to the neighbors. On the other hand the normally unused facilities restrain the demand for growth of the area.

. Loss of initial objectives. The stated objective of the FIES have increasingly been lost. The chamber of Commerce (Camara de Comercio), in an article strongly criticized the FIES getting away from its original objective, becoming:

- a) A place where occasional entrepreneurs perform illicit competition through the smuggle of goods, transforming the FIES into an enemy of free competition.
- b) A festive-amusing activity of a domestic character.
- c) A very expensive promotional means of the State bureaucracy.

The FIES represents the interests of a limited group of the import and export sector of the country and could be perfectly operated by this sector.

EXHIBIT 4.3

. The best alternative is to lease either totally or partially (by phasing). And to relocate the function into other area.

Finally, some recommendations in the case of a FIES privatization scenario are the following:

An examination of the area where the FIES and other privatization candidates are located permits to identify a level of complementarity which taken into consideration would enhance their real asset value.

The following are some of the different alternatives that could be proposed for the FIES:

a. To continue operations without improving the property. It has the disadvantage of opportunities foregone for subsidizing a function that could be provided by the private sector.

b. Total Divestiture of the FIES as it is. It has the advantages of changing the usage of under utilized resources to a higher and better use and generating revenues to the state. It has the disadvantage of producing the lowest possible profit in the liquidation.

c. To dispose of the real property in parts. This option has the advantage of distribute in a time span the divestiture. This permits the government to keep operation of the FIES while permitting the potential appreciation of the different phases of the development.

d. Leasehold for a fixed amount of time. This alternative has the advantage of distributing the potential income over a span of time while keeping the property of the land and future improvements.

e. A joint development of the state and the private enterprise. The state provides the land as its equity and the private enterprise develops the site to a new use. The government participates of the revenues and potential appreciation on the land.

f. To privatize the enterprise transferring the management. Has the disadvantage of keep running an obsolete

function and not giving the property its highest and best use.

Based on these alternatives, which did not pretend neither to be exhaustive, a study could suggest for example, a privatization method that suggests a joint enterprise government-private sector. Which intensifies the use of the FIES, keeping some space for the future. While developing the rest for a mixed use development with a private developer. The area for development which could be the middle area and the area of la Lechuza, could be accessed from San Benito by communicating the dead end of a Av. Las Palmas in the San Benito. This could be the first phase of the development. Then if successful the FIES could be either relocated totally to an area such as the new airport.

This would imply:

1. It is feasible to relocate the FIES to an area (for example, near the International Airport as suggested by the FIES president). This would require buses for transportation to the area in the days of the event. This alternative has been tried successfully in the past. The first FIES events had to have special lines to the event. In its beginning the Fair was served by these kind of public transportation since it was in the suburbs.

It would put a center of development for that area, such as the hotels, zonas francas, and other facilities being built there which have more to see with export import. A permanent event of El Salvador export inventory as suggested by FUSADES and the Chamber of Commerce would be a subject for further analysis.

The possibility of a space use intensification in order to leave the FIES in the area (subjected to a benefit cost analysis) but permit area for development. If the space is subsidized and use less.

The development of housing projects, (for the poor as well as markets.) the squatters provide labor for the surrounding

places)

Given the degree of complementarity (see section 2.26) among the FIES and other GOES properties, the development for the FIES should consider a joint development with other GOES properties in the area.

The Lechuza which surrounds the FIES to the west and south gives possibilities of access from other areas of the city.

To include the Handicraft market which now consists of 36 stores and a plot of approximately 2000 V² located between the FIES and La lechuza. It runs under the ministry of Economy and leases its stores at low prices. This area has been identified by the municipality for the development of a marketplace which would serve the west part of the city. A new approach with the private enterprise could be tried to develop such a marketplace. (there have been precedents of development of such kind. Marketplace Hula Hula, to be developed by Jimenez Castillo Arquitectos.)

Any privatization/divestment initiative in the area should take into consideration that its results would be improved if the military facilities were relocated to outside of the city³. The relocation of military installations outside the city has been proposed in the past by the GOES before and it appears more feasible because the war is likely to end. This scenario would increase the existing demand on the area, with the resultant of an increase in market values in which the government as a major owner of the land in the area would benefit. If military authorities were presented a benefit cost analysis of the relocation, acceptance might be likely since the land is worth millions which could be devoted to built new facilities. The present military installations are technically obsolete and are incompatible with the rest of the area (see appendix 4.1).

This case study has illustrated issues and possibilities vs current considerations. A benefit cost analysis of the strategies is outside the scope of this thesis.

SUMMARY.

The case studies presented evidence that the alternative focus for privatization analysis proposed in chapter 2 is important to be considered in the analysis of potential candidates. The current GOES privatization evaluation, does not identify at hand feasible candidates which could be relocated and exploited for their real estate potential.

. It ignores the opportunity cost to the GOES in subsidies for free land to institutions. Especially if they favor a reduced group of enterprises

. The existence of misconceptions and incorrect procedures threaten the current privatization effort because it is too restrictive and fails to realize the real property characteristics of the candidates.

. The GOES Privatization process does not evaluate real property potential for alternative uses which nor takes advantage of the ever changing real estate conditions.

NOTES OF THE CHAPTER

1 An area of the FIES has served to host for the past ten years the San Benito battalion. The Ministry of Defense had also overtook definitely the old parking lot of the FIES to built its permanent facilities for the Instituto de Transmisiones de la Fuerza Armada.

2 The fair is an institution that is in a period of evolution. The manager of the FIES, Mr. Maximiliano Figueroa as well as the Chamber of Commerce of El Salvador, predict that the Fair is going to be transformed into a place where specialized exhibitions will be hosted. This would involve the reduction on the need for space.

3 The military installations, established a long time ago in the east of the subject study area were planned to move out of the city. Some areas at the nearby Espino Hacienda, were designated for the use of the military, and this is known as a military development known as the "Hexagono". 7 years after this plan was proposed, just one military installation has been built in the area. A factor that might lessen the influence of the negative influence military installations is the increased prospects for a dialogue and an end to the conflict.

CHAPTER 5 THE PRIVATIZATION PROGRAM APPRAISSAL:

THE CONSIDERATION OF THE REAL ASSET VALUE

This chapter is an appraissal of the different privatization initiatives presented in chapter 3. It follows the guidelines drawn in section 2.3. It evaluates technical and political issues preventing consideration of SOEs' real property real asset value at least in the short term.

5.1 REVISE THE NEED FOR THE PRIVATIZATION PROGRAM.

The GOES privatization program has placed little emphasis on income generation via real property divestiture. Divestiture via real property was not considered when the GOES PAE was conceived. The PAE considered generation of revenues via higher taxation exclusively. In this regard Wisecarver recommended.

"That given the level of economic and social development of El Salvador aiming at achieving a reduction of public spending via cuts on physical and human capital... Does this constitute a responsible policy? If the answer is no, ...the imperative and urgent necessity of achieving a higher tributary collection, is therefore magnified. It looks like El Salvador does not have another option." [Wisecarver, 38].

Wisecarver's recommendation influenced the GOES's willingness to consider other sources of income generation besides tributary collection. It discouraged cuts in real property, therefore eliminating both the possibility of revenue generation via real property and the incentive to consider real asset value.

Wisecarver's recommendation contrasts with FUSADE's 1990 proposal to the GOES which advocated the use of real property as an alternative source of income generation. The basis for FUSADES claims were the high opportunity cost of holding idle real property resources; and the non-optimal utilization of real property in prime locations. This was the first document in El

Salvador to urge consideration of real asset value in privatization analysis.

The GOES aspires to be self-sufficient. The government relies on foreign aid as a source of revenue. However, the aid is in danger of being withdrawn. This creates pressure on the GOES to generate revenues, not only by taxation, but to use its own resources. After ten years, however, the government is overconfident given its dependency on foreign aid. There is no awareness of the increased prospects of an eventual pull back of foreign aid. This was acknowledged, in a private interview, high ranking official of a foreign aid agency, who stated that neither the government nor private enterprise show signs of understanding that in a short time foreign aid will be reduced significantly.

The government has previously chosen to ignore real property divestiture; however, this solution is presently gaining momentum. Exploiting the GOES own resources would mean putting the assets to their highest and best use. However, certain political and technical circumstances preclude this situation. This can be appreciated in various elements of their approach to the gathering of an inventory.

The emphasis here should be switched from the exclusive concern for the reduction of both the fiscal deficit and the size of the state, to the achievement of the highest and best use for government resources. There is a vast, idle RPP integrated by properties that are underutilized, undervalued, or surplus to any government need. As it stands now, the GOES's institutional real property occupies 4% of the national territory which is kept mostly vacant (not considering forest reserves or highway rights).

The lack of analysis of the real property potential might be based on the fact that Wisecarver's research was done before the current inventory. The only inventory available at the time was the Direccion de Contabilidad Central's (DCC) which conveyed a small real property inventory that is analyzed in section 5.8.

5.2 THE DEFINITION OF OBJECTIVES.

There is not a clear understanding nor a clear definition of objectives, and perceptions in the current privatization program. The definition of clear objectives is of much importance because, "the choice of privatization or divestiture techniques is generally a function of government objectives, the SOE's/entity/asset condition, its sector of activity and the country characteristics."

In El Salvador, the current trend is to evaluate activities exclusively based on the objective to reduce the fiscal deficit and to reduce the size of the state.

As mentioned above each program's objectives must be adapted to the special needs of each country. In this particular case it makes sense at the moment to look for candidates that following the objectives mentioned above could generate alternative sources of income for the government. This given the fact that in the transition of the restructuring/adjustment program the maximization of liquidation revenues and the intensification of the use of space by means of physical size reductions, fixed capital losses, might prove to be very effective in generating alternative sources of income. Then as the program begins to be implemented, increased productivity and economic growth could turn out to be more important objectives than short term deficit reduction and revenue generation.

In the GOES privatization scheme, sectorial interests tend to prevail over the overall vision, given the fact that there are different perceptions of the government officials involved in privatization evaluation. The interests of sectoral parties may prevail over the GOES objectives. This affects the evaluation of alternative uses of the real property held by SOE's, because inside parties tend to retain current usage. Input information for privatization analysis comes from upper and middle management within the SOEs/entities which are candidates for privatization. Therefore, management influences potential solutions, even if privatization efforts originate at

a high level. For instance, previous ISIC privatization research (see case study 4.1) was done taking into consideration the PROCAFE and ISIC interests. From the MAG perception it was better to keep property either for a posterior sale or to build its new facilities. From the GOES perception it might be better if as result of divestment the income resulting from the sale of the land could contribute to the GOES social programs.

The divestiture of the military facilities in the San Benito area would most likely increase the prices of land in the area which is mostly owned by the government. However, regardless of the benefits to society of eliminating an incompatible use in the area and the feasibility of relocation of these facilities. No action could be expected since there is not a centralized decision making that could persuade the military to relocate.

5.3 THE PRIVATIZATION PROGRAM PLANNING AND MANAGEMENT PROCESS

The overall privatization process has been poorly planned and managed since its announcement. The plan lacks clearly defined objectives, results and transparency consequently increasing potential opposition and endangering the process. The privatization process has been implemented slowly.

The first privatization candidates have not been successfully privatized in the eyes of the public. The Instituto Regulador de Alimentos (IRA), for example, was liquidated based on the rationale that it had not been operating for five years, draining 120 million colones from the budget. The IRA was accused of buying agricultural commodities high and selling low in addition to corrupt operation. However, the institution had a "popular image", which was tarnished by the opponents of the privatization program. They presented arguments ranging from unemployment (even if the benefits to employees equaled a year's salary) to rising food prices. Consequently, the opponents of the privatization program created an adverse atmosphere for the IRA liquidation. There was

a strong public debate, union strikes, and even threats by some U.S congressmen to cut the U.S economic aid if the IRA case was processed. As a result of these pressures, the Minister of Agriculture was called before the National Assembly to clarify the legality of the IRA liquidation. Some government officials avoided responsibility by not taking sides on this issue and saying the central government did not know whether this liquidation was legal. The IRA liquidation proved extremely unsuccessful at gaining popular support for the privatization program. Before proceeding with the liquidation of IRA the GOES should have successfully privatized the other candidates. However, the GOES's first candidates have not been successfully privatized because of both low of viability and the aforementioned pressures.

The IRA controversy provoked hesitation by the GOES on how to proceed with the privatization program. President Cristiani stated to the nation in a televised speech that no further liquidation of institutions would be made. Cristiani stated that the privatization program would issue and sell shares of public enterprises and banks. The exclusive consideration of this method prevents SOE's real property achieving real asset value (as is further explored in section 5.4).

The government has dealt with the privatization program from a purely philosophical perspective. This standpoint contrasts with chapter one, which recommends turning to the real issues focusing in aspects such as the satisfactions foregone for holding under utilized property, the necessities of investment in other areas, and the real cost of subsidizing obsolete enterprisese by means of free space.

The lack of a concerted, well-planned effort is hurting the privatization program.

Other privatization candidate cases that have been problematic in terms of showing success are:

a. In 1986, disposition of municipal land reserved for parks to private developers --some with connections to the

ruling political party-- created apprehension on the community against the Government as land seller. These land dispositions were condemned by most citizens thus impacted negatively on the privatization effort. The action created a bad precedent for any governmental action involving the disposition of land to third parties. The municipality made little profit. Land was sold at its original value, which was sometimes 300 times less than the market price. The under-priced transactions were revised and the land re-nationalized. The latter does not create a good environment for investment by the private sector before the fear of re-nationalization, influencing negatively the choice of methods.

b. The Presidente Hotel (see case 4.2) was the first property targeted for privatization. This was an obvious choice since governments should not be involved in a hotel business [Cristiani]. After six years on the market, the hotel has not yet been sold. Reasons range from insufficient efforts the government to the lack of a market for hotel real estate.

The privatization decision-making process regarding this hotel has always been based on the expectation that if tourism expands in the country this major hotel will be necessary. Therefore the GOES should not dispose it for another use. This has led to lost opportunities. In 1989, for example, there was short demand for hotel (65% vacancy rate) and the demand for apartment and office space in the area was high (see section 4.2). (A consequence of the 1986 earthquake and the continuation of the war). A research study at the time estimated that the hotel's second floor could be remodelled and converted to office space. However, CORSAIN did not take advantage of the opportunity. The hotel could have been converted to office space and condos, with a club and convention center in the common facilities. At the time, it was more feasible to divest the property to a potential buyer who had in mind converting the hotel to whatever the market required.

There is a bias towards maintaining ongoing uses (as

mentioned in section 2.27). This bias affects the free flow of market forces that would otherwise identify the right moment for building again a major hotel. Meanwhile possible benefits to the state from changing hotel uses could have included the following: a) revenue generation; b) avoided operation losses; and c) finance other necessary activities with funds from the nationalized bank system, which were used to finance increasing space offer in the San Benito area. The later has resulted in surplus space in the area and lowered market values of real property.

5.4 THE ELIMINATION OF DISTORTIONS

The GOES must decide whether core and noncore enterprises will be sold, liquidated, or rehabilitated. This would result in the SOEs fending for themselves, clarifying their true situation. This should be achieved by eliminating subsidies or new public investments. The privatization program distortions are the following:

5.41 Opportunity Cost.

The current privatization program lacks consideration to the enormous opportunity cost caused by holding the GOES idle portfolio. This is negative:

a. In view of the country's major social and economic goals, the first priority should be the execution of socially desirable projects and/or the rehabilitation of the deteriorated infrastructure. At a time when expenses are steep, funds scarce, and austerity encouraged, the Government cannot afford the luxury of holding excess real property. Otherwise this cost is transferred to the taxpayers, either through higher government services costs or by essential societal services foregone.

b. It limits private sector access to vacant or under-utilized properties that otherwise could be used more efficiently than by the Government. The static management of

the idle RPP signifies a poor utilization of the country's resources. This results in a high opportunity cost for the economy, especially in light of the existing demand on these resources by the private sector. This contradicts the GOES postulates as stated in section 3.1. In the past, real property assets have been accumulated without regard to the GOES needs. This was not obvious in the past but in difficult times institutions tend to look at existing resources.

5.42 Space Subsidies.

The current privatization program does not account for the opportunity cost of subsidies given in the form of free space or subsidized space to SOEs (see section 1.4).

On subsidies, Jose Marques, a senior economist at the World Bank, states that "it is crucial that during the period of adjustment, the GOES keeps or expands its social programs directed towards the poor. This can be achieved by an increase in the recovering costs on the ones which possess more income, privatizing social services, eliminating general subsidies that generally benefit more those who do not need them." [Marques: iii].

If the Feria Internacional de El Salvador (FIES) (see case 4.2), for example, had to pay rent on the open market it would cost 19,600,000 colones yearly, assuming an average rent of 40 colones a month per square meter, for similar space in a comparable location. Considering the fact that the FIES shows a balance of only 300,000 colones every two years, under this scenario its functions would become unsustainable and it would have to close. In this case, maintaining the subsidies prevents real asset value from being considered by maintaining an ongoing use that would be impossible under normal business practices. According to Max Figueroa, General Manager of the FIES, there are similar events of this type run by the private sector in countries such as Colombia or Germany, for example, which have proven efficient and are not subsidized [Figueroa].

Free subsidies in the form of land or facilities given to SOEs that offer services for sale or lease to third parties benefit very limited groups as seen in the case of the FIES.

Subsidized space implies inefficiency in the use and allocation of space resources, along with distortion of real estate market prices, and highest and best possible use. Free allocation of resources by market forces is prevented because the private sector and/or the community limited access to available land.

The question of subsidies, relates to under-utilization. At one time the departments at MIT, were not accounted for the space they used. Space was wasted or used in excess to departmental need. Some departments were justifying unnecessary functions in order to keep some space [Kreon Cyrus].

The fact that SOEs can operate only because of space subsidies leads to a distortion which should be eliminated (see section 1.4). Even when subsidies are deemed necessary, they should be evaluated, since they provide a benchmark of opportunities foregone. The FIES, for example, uses its space once every two years for a period of 17 days. In the FIES as well as in other non core SOEs, the size of director's offices occupy more than 300 square meters. If the enterprise rented a space of this size in the open market it would pay 288,000 colones for each office yearly (80 colones per square meter monthly). This represents income foregone because it cannot rent this same space to third parties. This situation contrasts with some government offices where employees are given 3 square meters.

Subsidies for space in noncore government SOEs contrasts with the high rents that some critical government institutions pay for their office space. The Ministerio de Hacienda, for example, occupied some of FIES installations after its facilities were destroyed by the earthquake in 1986. However, the institution was forced to leave in 1990, and now rents expensive office space.

The Hotel Presidente (see case 4.2) management does not pay the government for its space, and yet still carries losses. This has lessened pressures for good management and produced lost opportunities as a result. The hotel is said to not produce losses. In reality there is a high under-utilization and practices such as not charging government institutions or officials for the use of the facilities are common. This was not the case when the Hyatt Regency operated the hotel.

Subsidies are also an issue in the PESPP program. It is the PESPP's policy to sell land at market value. However, PESPP does not currently recognize the real asset value of land that is transferred. Under the scenario shown in Appendix 5.1 assumptions, most of this program will have to be subsidized. As a result if the PESPP expected quota ceiling is maintained most urban land disposition will be highly subsidized. This subsidy may come as a result of the consideration of the end-user's low-income economic situation. However, the land's real asset value is not considered, nor is its highest and best use. In cases where the land is located in prime development areas its transference may benefit a limited number of families, as opposed if the land was sold at a price determined by its real asset value price, and revenues would spread among more families. The fact that the PESPP transactions will have to be subsidized is acknowledged by a publication which analyzes the GOES's housing program ¹. In the PESPP program the real asset value of the land is not recognized for technical and political reasons. This is significant because the program has high priority over other programs (see section 5.4).

5.43 The value in use vs value in exchange tradeoff.

The current GOES privatization program does not evaluate the tradeoff of the use value and exchange value of real property. This leads to a distortion in the evaluation of potential opportunities. In the SOEs analyzed in the case studies, the use value is way below value in exchange as

observed in the case 4.2. This residual approximates the opportunity cost. The lack of consideration prevents the consideration of the real asset value and the highest and best use of real property.

5.44 Investment for Physical rehabilitation and Potential for Alternative Uses.

The core and non-core SOEs in El Salvador need rehabilitation. The core SOE's that require rehabilitation for future privatization includes: railroads, airports, ports, utilities, post- and tele-communications, and government industrial installations (such as the free trade zones). However no attempt by the government has yet been done to privatize some of these SOE's/facilities's real property assets such as warehouses, terminals, or air rights which might offer potential for other uses. Some examples follow:

a. The Comalapa International Airport in El Salvador would be very desirable to privatize from the government's standpoint. However, the potential impact is high and the opposition strong. Nevertheless, real property surrounding the installations could be leased for development of warehouse facilities or light industry. Also warehouses now used by the airlines could be leased.

b. The Comision Ejecutiva Portuaria Autonoma (CEPA) public entity in charge of handling the port of Acajutla has property surrounding the port that has added value. However, there is no real compensation for the appreciation. The government would benefit from leasing the land. In this case efforts have been made to create a joint venture with the private enterprise unsuccessfully (see also section 5.4).

c. San Bartolo, a free trade zone, has been targeted by the government for privatization as an ongoing use unsuccessfully. However, the scheme does not consider the real asset value of San Bartolo's real property. The real property has potential for alternative uses for the following reasons:

- . The free trade zone facilities were developed about twenty years ago in the sugar cane fields close to the old Ilopango International Airport. The closing of the airport in 1976 to be used exclusively for military purposes affected the prospects of attracting investment to San Bartolo.
- . The free-trade zone is now surrounded by Soyapango, a rapidly growing urban center of the AMSS which has increased its population from 100,000 to 500,000 in seven years. This growth has created demand for other uses in the area. The space, while still interesting for productive facilities, might have reached the point of having potential for other uses, such as supermarkets and shopping centers. The private enterprise has been developing warehouses and factory space in the area to house other functions, such as shopping centers.
- . Six new free-trade zones are being developed in various parts of the country. These sites will offer alternative sites at lower rent, close to the ports and the Comalapa International Airport.

Most non-core GOES's SOE's are not ready for immediate privatization because of their poor physical condition. The GOES, regardless of its financial constraints, has been rehabilitating these enterprises. These investments have not proven cost-effective and may never be fully realized. Many physical rehabilitations have been done on properties with potential for alternative uses. Such investments raise the government's expectations, both on a high potential price and to keep the SOEs current use. This precludes considering alternative uses for the real property. Potential investors may have very different views on how to rehabilitate and/or change uses of the real property occupied by the SOEs. Consequently, they may not be willing to pay according to the GOES price expectations making it difficult to close

transactions. An costly physical rehabilitation of the Hotel Presidente, for example, for which figures could not be obtained was done by the government. However prospects for the hotel being sold are weak. The rehabilitations have been made based on an expectation to increase the SOEs attractiveness to potential investors, so that the government could not be criticized for disposing national assets at low prices.

5.5 SOE'S REAL PROPERTY EVALUATION

Based on the results of Chapter 4, the current privatization program has not included for those SOEs and/or institutions that have the following characteristics: their real property is underutilized, subsidized, undervalued, and/or surplus to the SOE's needs; the real property has a potential for a higher and better use than the current one; the real property characteristics might enhance the real asset value of other privatization candidates; and the real property is given non-intensive-use in prime development areas and/or it is incompatible with uses in the surrounding areas (see chapter 4 for further information). The current privatization scheme lack of consideration to the principles proposed in the guidelines prevents the achievement of real asset value and highest and best use of the real property held by SOE's and public institutions.

5.6 DETERMINE THE PRIVATIZATION METHOD.

The determination of future ownership depends on government objectives and market conditions. The GOES privatization program is unclear about the implications of the methods chosen. Raising revenues, for example, is one objective of the GOES privatization program. However, the GOES's exclusive selection of a privatization method for issuing and selling shares, determined by external pressures, prevents the achievement of such an objective. The GOES has limited in effect the privatization program, by precluding the possibility of

liquidating obsolete government functions, closing or selling obsolete SOEs, and selling or leasing their underutilized assets. Consequently, preventing the consideration of the real asset value in those cases where the real property held by the SOEs/entities with potential alternative uses.

In Chapter 4, various institutions were analyzed for their potential alternative real property uses as opposed to current usage. If privatized as ongoing uses, these SOEs will not fully realize the real asset value.

Privatization methods such as leasing, joint ventures, or the participation of the private enterprise in the rehabilitation of SOEs have been tried unsuccessfully in the past. The effort to create a joint venture with a private firm to develop a free-trade zone which would utilize publicly-held vacant land owned by CEPA in the Acajutla port failed because of the unattractive interest rates ².

The transference of real property assets to the private sector by means of divestiture is part of a privatization program, but is also a main activity in management of the real property portfolio. The GOES gives to privatization and divestment a high priority. These two options, however, just two among the possible asset management techniques that the government could use in order to manage the real property portfolio in a coordinated fashion. The techniques include acquisition, leasing, space use-intensification, relocation and reshuffling of resources from one institution to another or within the same institution.

The lack of consideration of other alternatives besides privatization or divestiture prevents evaluating the aforementioned techniques as part of a combination of alternatives. In the Feria Internacional (see case 4.2), for example, the real property could be partially privatized, and the current facilities given intensified uses while gradually developing the rest of the property to mixed uses. Otherwise, the excessive emphasis to privatization or divestiture prevents

the consideration of real asset value of real property which has potential for mixed alternatives that could gradually increase this value.

5.7 INSTITUTIONAL FRAMEWORK OF THE PRIVATIZATION PROGRAM

Two contradictory institutional schemes exist for the privatization process, and both have political support (see section 3.2) The first, a loose decentralized scheme, considers that each SOE is thought to be capable of starting its own privatization process, and it presupposes that they know how to proceed. The point is to prevent the formation of a privatization "Tzar" [Zablah, Minister of Economy]. This approach contradicts the successful privatization practices in other countries in which the evaluation of privatization candidates has been made by independent parties and an independent organization has coordinated the process.

The second, the Privatization Commission scheme, is unlikely to be promptly implemented. The commission has the support of USAID, but there is insufficient interest within the government constitutencies to give it enough power, at least in the short term. The commission has been under attack from within the government since its inception. A minister, referring to the commission states "there are 17 barons who would not let anyone take power which makes the process of decision making really hard." A high-ranking officer of the Commission acknowledges that the commission is under attack: "There seems to be interest in wanting us to look bad before the government and the USAID". Added to this, the Commission does not seem ready to be given full power, nor does it have a privatization plan. The limited resources of information in real property inventories have not yet reached the commission.

In view of the above, the loose decentralized will prevail for the short term, since the privatization commission might not be operational soon. Under this scheme, each SOE is expected to start its own privatization process independently as mentioned.

The other privatization-related alternatives, such as the PESPP and the divestiture of land, are not coordinated with the privatization commission. Therefore the privatization initiatives are based on the proposals of the interested ministries, and not on a concerted effort. This creates the following problems:

a. Privatization initiatives are evaluated in isolation in this scheme. The scheme therefore fails to detect opportunities for joint analysis of privatization candidates, such as the FIES and la Lechuza which belong to different ministries, based on their real property characteristics such as complementarity. This consequently prevents the recognition and/or maximization of their real asset value as the evidence in case study 4.2 shows.

b. The interests of sectoral parties may prevail over the GOES objectives. This affects the evaluation of alternative uses of the real property held by SOE's, because inside parties tend to retain current usage as explained in section 5.2. This was evaluated in the ISIC case study (see case study 41). In the case of SOEs such as the FIES, La Lechuza, or Hotel Presidente, if privatized with efforts that come from the entity itself, they would be kept in their current use. The case of the military installations mentioned in section 5.2 provides another example of sectoral objectives prevailing over the government objectives.

c. The decision-making process for privatization of the GOES is reactive, responding to political pressures rather than technical arguments, and therefore ignoring sound asset management practices. This is a result of the loose and uncoordinated decision-making process worsened by the haste of the PESPP program, which contrasts with the slowness of the privatization program. The combination of the aforementioned situations does not create a good environment for decision-making, especially in the absence of a global vision, coordination among different initiatives and mechanisms for real

property management. Consequently the PESSP program tends to prevail.

d. Sectoral interests of different groups, programs, or government institutions may prevail over the overall interest of the government. For example, a program which is receiving more attention at a particular moment might take precedence over other equally important programs. Therefore the decision-making process is done based on the need to satisfy the sectoral objectives of a particular initiative rather than to satisfy higher-level objectives such as better use of resources. Some examples are:

- . In the current privatization decision-making there is no mechanism to decide priorities for particular pieces of land. Two or more initiatives may be studying the feasibility of privatization of the same lot of land. Given the lack of coordination the initiative that first identifies a use for the land, regardless of the its highest and best use, would privatize the property. This ignores the real asset value. A lot of land located in Santa Ana, for example, which was first designated by the PESPP program for a housing project, was then also proposed by another initiative to be leased for the development of a free trade zone. Because the PESPP initiative identified the property first, the lot was assigned to this initiative regardless of the fact that the highest and best use of the land is in the latter alternative.
- . There is conflict of interest within institutions. CORSAIN, for example, was until 1990 the body in charge of privatization, but lately also distributes land to the PESPP program as one of its functions. The haste of the PESPP program creates pressure to assign properties to the housing program, which prevents properties being given to other productive activities. Given the short span of time and the lack of accurate inventories, this could mean giving away non-registered government owned land e.g. the

PESPP program will grant title to the those living on the 10 hectares of land in the El Manguito community. This land has not had a registered owner for many years. However it might be part of a property the government bought in the 1940's as part of the El Salvador Country Club.

5.7 REAL PROPERTY INVENTORY AND MANAGEMENT STRUCTURE.

Having access to systematic knowledge about current real property holdings is a necessary condition for large organizations in order to maximize real asset value. The current privatization process takes place within a pattern of widespread mismanagement of the GOES's RPP which includes the lack of accurate inventories. This creates technical and political barriers to the consideration of real asset value in the near future.

The lack of both a real property management tradition and theoretical knowledge creates no incentives to achieve the real property highest and best use. For example, there is no incentive to recognize the opportunity cost of holding real property or subsidizing free space to SOEs, as examined in section 5.32

Estimations of the real property inventory have been historically based on the reports of the "Dirección de Contabilidad Central" (DCC), the entity in charge of the valuation of real property assets in the national budget. The figures of the DCC inventory shown in appendix 5B provide an extremely undervalued picture of the GOES's RPP, as compared to the inventory presented in Chapter 3. The insufficient and under-valued data of the DCC inventory hide the exchange value of most properties and do not permit the evaluation of their restrictions and possibilities. Given the fact that no inventories were available in the past, the DCC inventory, despite its innacuracies, has been the basis for research studies in the determination of policies in real property.

The lack of both accurate inventories of real property and a real property management tradition, mentioned above, are important to understanding why real property has been ignored by researchers working on the structural problems of El Salvador's economy in general, and on the size of its public sector in particular. For example, major research studies such as Harberger and Wisecarver, which were the basis for the policies of the new government, overlooked the implications of an idle RPP and recommended that no actions should be taken to reduce fixed assets (see section 5.1). As a result, the GOES's five year plan mentioned nothing about the planning and management of its real property resources. The idle RPP was regarded as a vital part neither of the GOES restructuring program nor of the privatization objectives.

The RPP potential has finally been accounted for, because of the results of the new inventory. Since the inventory started producing results there have been leaks of information e.g the National Assembly asking for partial results. This was the reason for many of the pressures mentioned above.

Despite the importance of the new inventory stated in Chapter 3, it is unlikely that this might be an accurate tool for privatization decision-making in the near future. This is especially true with regard to the real asset value and determination of the highest and best use. This conclusion is based on technical and political considerations such as the following:

5.71 Technical considerations:

a. The lack of a centralized system of real property information results in a lack of a global perspective. Privatization involves, by necessity, several government constituencies which must have access to information. A centralized system could be accessed by the different privatization programs and constituencies involved in determining the use of the public sector real property.

b. The information on real property is held in different institutions with uncoordinated functions and obsolete methods of gathering information. Real property legal status, value, or even existence is not accounted for in these institutions' accounting departments. The Direccion de Contabilidad Central (DCC), for example, is supposed to provide accurate, up-to-date inventories. However, many government properties are simply not in its books as a result of problems of logistics and discipline.

c. Attempts at changing the real property management structure are limited by the lack of organizational capability or technical expertise in managing real property.

d. The VMV inventory has focused on the PESPP program exclusively. This inventory sectoral focus, added to its innacurate information, produces the following problems:

- . Failure to provide complete real property information which would be helpful for strategic decision making in privatization. The current inventory has an exclusive emphasis on vacant land. This means that all other information, such as buildings and land in use, which has also been gathered, might be lost in the process.
- . Biased information, which does not help privatization or other real property management decision-making processes. Therefore, properties which have potential uses other than housing may end up being given away to housing projects because of this current inventory focus.
- . The lack of transparency of information. No specific details about each property are presented because it might not appear politically convenient to show that a GOES institution owns completely unused properties such as a large villa in Coatepeque Lake.

e. There is a lack of a coordinated central initiative on the valuation of real property components of the inventory. Each ministry and government institution is expected to make the valuation of their own properties ³. The argument for each

institution updating the data on "their" real property is that each institution is expected to arrange its own house. Each division will take care of updating the real property data, and this information will be transferred to the DCC. This scheme is unlikely to succeed given that: a) institutions lack the necessary technical or human resources, and land registration procedures are obsolete; and b) people use property that does not belong to them, and there are plenty of overlaps and undefined borders among properties.

Most likely then, there will be no update of the information or it will be very poor. The process will not verify the market value information property by property. The VNV was planning field research on each property but under the MIPLAN now this idea has been abandoned.

Valuation is an important process in privatization. This includes valuation at the level of the whole inventory and valuation in the particular case of each privatization candidate. Within the latter the current scheme of valuation presents the problem that privatization criteria for the valuation of the real property assets have not yet been developed. In this country the current method of estimation for valuation purposes according to DGP is based on the estimation of the replacement cost (as mentioned in chapter 2).

- . Under the current methods of DGP, the cost of deferred maintenance is not estimated and the figures only consider parameters of current costs of a square meter of a similar type of construction. A factor of depreciation is then applied. Say the building is 25 years old and the expected life horizon is 50 years, the building would be depreciated of its replacement cost 50%. This formula does not consider the growing physical obsolescence resulting from deferred maintenance, which depreciates the value much more.
- . Space currently used by the SOE might be in excess of the needs of the new entity. However, no post-occupancy

evaluation has been executed. Further assessment of both the post-occupancy-evaluation and replacement cost methodologies are beyond the scope of this document.

The current method of valuation, replacement cost, should not be considered in the estimation of an institution/SOE's worth to the GOES. The GOES does not replace the facility, so this should be instead the concern of the new entity. What is important from the GOES's standpoint is the NPV of an SOE's current income, which could be compared with the opportunity cost of those facilities, determined by the market value (as explained in chapter 2).

Most government officials agree that there should be an institution to maintain a central inventory. This is the case of the Ministry of Hacienda. Unfortunately, this institution has demonstrated strong resistance to changing the current procedures for real property management.

5.72 Political considerations:

a. The current narrow focus of some GOES officials for whom the gathering of a real property inventory is the last step in the management of the public sector assets. GOES officials, because of their lack of background information on real estate management, do not have an understanding of real property importance in relation to government policies. GOES officials adhere to traditional methods of accounting.

b. The project has not interested GOES institutions. Therefore, it lacks importance at the strategic Consejo de Ministros level where the purpose of this information is not well understood. The lack of political support results in the poor deployment of resources for the inventory. This has resulted in a slow process characterized by lack of access to hardware and people (see appendix 5.B for details) and by the lack of prompt reports of the institutions concerned. As of June 1991 the inventory had already taken two years and it is

far from completion. Institutions took very long to respond and most did so wrongly or based on incorrect ideas of what is their property.

c. The gathering of information has occurred under two ministries. There has been repetition of activities and data in the VMV inventory has not been taken into account in the MIPLAN inventory, e.g. the legal status of the property.

d. The inventory is most important under the current "El Salvador Pais de Propietarios" program given that there will be an immediate process of legalization of real property. In some cases the own government may not acknowledge ownership and will give away land that belongs to the nation as a whole. This is most problematic for the government, because there are at least 3000 properties in the hands of the State. Most of them have not been valued, and in some cases their existence has not even been acknowledged.

The inventory information should be aimed at identifying also real property which has potential for divestment. It is unlikely that given the lack of real political support and understanding, the inventory efforts will achieve satisfactory results or be the base for successful uses. This prevents the real property held by SOEs achieving the real asset value.

SUMMARY.

Given the technical and political obstacles discussed here, it appears unlikely that the privatization effort will be able to recognize either the real asset value or the highest and best use of the assets which are candidates for privatization. In summary there is need for an accurate inventory as the first key step to the establishment of sound asset management practice. The current institutional structure in the management of RPP does not allow for sound asset management practices to take place in the privatization process.

The current pressure for the distribution of land by the

government to the housing programs, the haste of the PESPP program, and the slowness of other programs, may, in the absence of a real asset management policy, prevent the consideration of the real asset value, and the achievement of highest and best use of real property.

Government decision-makers and researchers underestimate or ignore the real property portfolio's importance as a most sizable and valuable but wasted resource. The lack of accurate inventories hides the idle real property potential. This has affected research studies and has resulted in the lack of political commitment to the consideration of the real asset value. As proposed in Chapter 1, this thesis considers the cost of subsidies in the form of free space to SOE's, and the evaluation of the opportunity cost of holding real property occupied by SOEs.

NOTES OF THE CHAPTER.

1 This publication states that "Even though the State may subsidize families on the acquisition of housing, this would not resolve the problems of more than half a million families in extreme poverty. In any case, the privatization would mean a high acquisition value, that even though there is a subsidiary component is not reduced effectively" [Fundabal,].

2 The rate of 19% is unattractive in relation to other countries in the area which subsidize the interest rate in the development of free trade zones.

3 There is a pilot plan project to create the divisions for gathering the inventory in the following five ministries: Public Works, Health, Education, Economy and Agriculture.

CHAPTER 6. CONCLUSIONS AND RECOMMENDATIONS.

This document concludes that for political and technical reasons the process of privatization of the Government of El Salvador is unlikely to occur in the near future, in ways that would recognize the real asset value or the highest and best use of the real property held by public institutions and state owned enterprises. However, evidence from an isolated case shows that taking into account real asset management practices might succeed in some cases in the current privatization process. There are windows of opportunity for governments looking at their real assets in a new manner; they could provide an alternative source of potential candidates that could be privatized successfully at low cost and high benefit for society.

This study showed the need for a privatization evaluation that takes into account real asset management practices. Privatization and divestment are just two among the possible asset management instances that the government could use in order to manage the RPP according to sound asset management practices.

Current processes of privatization for the following technical and political reasons neither consider the real asset value nor achieve the highest and best use for the real property held by the SOEs:

1. The privatization experience worldwide does consider real property in only an incidental manner. No examples were found to document changes of uses in the real property of the SOE's, nor of SOE's identified as potential candidates for privatization because of their potential highest and best use as opposed to their current use. This thesis concludes that real property, from a strategic and tactical standpoint, is not regarded as an important consideration in current privatization of SOE's analysis.

2. The current GOES privatization scheme has not accounted for various SOEs or institutions that have become uncalled for as a result of redefined government objectives and have the following characteristics: the space is underutilized, subsidized, undervalued, and/or surplus to the SOE's needs; the space has a potential for a higher and better use than the current one; the real property characteristics might enhance the real asset value of other privatization candidates; and the real property is given non-intensive-use in prime development areas and/or it is incompatible with uses in the surrounding areas.

3. The current institutional structure in the management of RPP does not allow sound asset management practices to take place in the privatization process:

- a. There is lack of a global vision and coordination among different initiatives; therefore the PESSP tends to prevail. The program of land disposal for income and the privatization of SOEs have this in common. This occurs in the absence of a real property management mechanism.
- b. A program which has recieved more attention at a particular moment might take the initiative over other programs which might be equally important.
- c. GOES privatization decision-making is reactive and not proactive --responding to political pressures rather than to technical arguments, and therefore ignoring sound asset management practices.

4. The GOES privatization process takes place within a context of widespread mismanagement of its RPP characterized by:

- a. Lack of accurate inventories on real property holdings hides the idle real property potential, and prevents the achievement of its real asset value. It makes research studies difficult; it precludes political committment to the consideration of real asset value. The sectoral orientation of the current inventory restrains its application to the privatization. The lack of a centralized system of real property information produces a lack of a

- global perspective on how to manage real property to achieve its real asset value.
- b. A lack of research and understanding of real property management theory and inadequate accounting practices hide or distort the opportunity cost of holding an idle RPP. This results in Government decision-makers and researchers underestimating or ignoring RPP as a most sizeable and valuable, but often wasted resource.
 - c. The current process lacks the incentives to account for the opportunity cost of holding real property or subsidizing free space to SOEs. The implications in terms of opportunities foregone to society and for the country are enormous:
 - . The opportunities foregone from holding under-utilized assets, at a time when the first priority should be the execution of socially desirable projects and the rehabilitation of the deteriorated public sector infrastructure.
 - . The competition for scarce government resources produces land scarceness in the face of increasing pressures on the public sector's RPP from both the real estate developers and squatters.
 - . The inefficiency produced by space subsidies to SOE's creating under-utilization and distorting the evaluation of SOE's productivity levels.
 - . The need to create alternative ways to generate income to the public sector in order to offset some of the negative effects of the PAE as opposed to the exclusive emphasis on tributary approaches.
 - d. It affects the privatization and divestment strategies and/or creates barriers to the identification and evaluation of potential candidates.

RECOMMENDATIONS:

From a personal view the following recommendations are proposed to refocus the current privatization program based on the following rationale:

1. There is a need for mechanisms that create the perception of the urgent need to generate a political process to rationalize the planning and efficient use of the public real property assets. A revision of the following practices is recommended: The opportunity cost of holding real property and the subsidies to space. The analysis of the needs for space in the SOE's should be driven by considering space necessities as in the open market like any other private enterprise, not subsidized by the state.

2. The proposed scheme must revise the methods of real property evaluation of privatization candidates to consider the possibility of alternative uses for its real property resources and their possibilities for relocation. This would replace the current scheme, which is based on the exclusive consideration of real property's ongoing use. This prevents achieving the real property's highest and best use. The analysis of creative and profitable solutions, such as market modifications or joint developments with adjacent properties to take advantage of the ever-changing real estate conditions is encouraged.

3. Management action on these forms of use of real property is necessary because of the following:

- a. The GOES objectives should prevail over the sectoral objectives of all parties involved.
- b. Research in the field must give more importance to the evaluation of the privatization candidates from a real property standpoint.

4. The creation of an inventory would help as a decision-making tool in order to identify real property occupied by GOES institutions or SOE's, its restrictions, and its opportunities. Given the urgency of privatization and divestment, this inventory is needed for practical reasons in the short-term. It

is, therefore, most important to intensify current efforts in the generation of the VMV inventory to transform its sectoral focus and update information such as market values. The following actions are suggested:

- . Give attention to legal status. Otherwise this will result in costly mistakes, as in the ISIC privatization, or lack of identification of potential opportunities for real property.
- . Update inventories accurately and include information which is relevant to privatization evaluation such as a portfolio list of potential candidates.
- . Consulting groups should consider the potential importance of real property case by case and not rely on distorted accounting figures.

5. At this point, it is important to suggest that the privatization/divestment effort proposed by this document be an integral part of an overall approach to the planning and management of the GOES's RPP. Therefore, a merging of the separated focus of privatization and divestment processes into a joint vision which unifies these processes is suggested. In the context of the GOES, this could be achieved by means of the creation of a real property centralized think tank which connects under a common umbrella the management of the RPP and all the current isolated GOES initiatives. Having a central decision-making body that would evaluate whether real property assets should be privatized, divested, acquired or donated to social programs would benefit the GOES in the following ways:

- . Coordinating the decision making process which controls and plans the use of public sector real property.
- . Keeping a global perspective and interest as opposed to sectoral interests.
- . Centralizing expertise in the area, helping to create an efficient decision-making process.

- . Determining potential opportunities if the real estate committee participates in the Government's full planning cycle.
- . Monitoring real estate matters, avoiding deviation of the attention of the GOES from its primary line of activities.
- . Overseeing government interests over the sectoral interests - ministries, institutions, or particular groups - to achieve the highest and best use of resources, rather than keeping them in their current use.

Some recommendations for the privatization effort institutional structure are:

- . To include in the privatization research teams, a member with a real property management experience, to evaluate potential strategies.
- . To redefine existing methodologies to include the possibilities of analyzing real property concerns.
- . The establishment of a real property strategy within the public sector connected to the GOES current privatization initiative. This would centralize decision-making and make candidate selection and evaluation more efficient. This should eliminate bureaucratization and coordinate the different real estate activities of the different government institutions.
- . To generate the political process to give these considerations priority among the privatization program.

An understanding of the aforementioned factors is fundamental to influencing decision-making policy, which should emphasize the importance of changing both conceptions and practices rooted in the system, to produce efficient management of real property. This must include the creation of the mechanisms necessary to implement the policies of divestiture decided upon. Without political determination, and understanding of the importance of physical factors within development management and planning, the

above recommendations would neither gain priority nor be successful. This study stresses the importance of using publicly held real property in the best possible way, to make it work for the state and the community.

This thesis has covered new ground and is quite broad in scope. Few sources could be found to treat the topic directly from the proposed standpoint. Thus, there was a need to assemble a bit of theoretical and practical information, and to delineate the domain. For this reason, the topics have not all been treated at the same level of detail. Emphasis was given to the different institutional perceptions about real property. This work is considered to be a first effort in the long-term goal of supporting El Salvador's government in the development of policies and strategies for the transference of its services or assets to the private sector. Substantial effort went into the gathering of isolated bits of information to generate the case studies. The many loose ends might serve as further topics for research in their own right. Their coming together in this thesis could serve as benchmarks for future work.

building was built having in mind a public institution client, with the arrival of the new government the transaction stopped since the potential acquirer was a first candidate for privatization and it was an expensive building in those particular circumstances. The building is running under an excessively accelerated process of obsolescence because both, its lack of utilization and the continuous attacks to the building with damages that had not been repaired. Military corps are installed in the top floors, because of the building strategic position.

8) El Espino hacienda

It has an area of 996 Ha, or its equivalent of 12,000,000 V2 is now worth between 250 and 300 colones a Vr2, therefore it has a market value of 3000,000,000 colones. The land was declared at book value at 50 cents a Vr2 when confiscated from its owners by the Agrarian reform intervention in 1981. Some of this rural land intervened was held in pockets within major areas of urban development.

Current status: The land legally belongs to ISTA, and is used as a cooperative manner as a coffee farm. This land is under intense debate about what to do with it. Last year, after a long legal process, started by the former owners, the court declared it the property should be given back to them. A public debate started, agricultural communities beneficiaries of the agrarian reform outraged, and began a campaign of public pressure (even threats). This motivated the intervention of the Minister of Agriculture in order to look for an alternative agreement in which the beneficiaries kept part of the property or the benefits of its sale, a major part was given back to its former owners and around 90 Ha were kept as a reserve land for park. This land is of utmost potential for the AMSS urban development because of being located in between densely populated areas.

9) Museo Nacional David. J Guzman.

Represents an amenity in the area, it uses a plot of land owned by the ministry of Public Works.

10) Ministry of Foreign Relations.

Old facilities of El Salvador Country Club. The facilities of this ministry have a surrounding land that is not utilized which is excessive to the institutional needs and necessary from the standpoint of government image exclusively. This land could be evaluated in the future as a park, scarce in San Salvador nowadays.

APPENDIXES

APPENDIX 4

State Owned Enterprises/entities in the area.

Military School and Estado Mayor.

These facilities had been long planned to be relocated to the area of El Espino {5}. As mentioned before, given the present situation they represent a potential serious threat against the security of surrounding neighborhoods and interfere the normal circulation of traffic in one of the main streets of the city. It has been a long desired goal of the GOES to relocate all military facilities out of the city but a discussion of the future of these military installation had always been a tabu specially in these recent years.

- a) The military installations which as a result of the 11 year old conflict, have been the strategic targets of various attacks from active guerrilla groups, with the following negative effects:
 - b.1 Damages to surrounding facilities such as a gas station, a medical clinic, restaurants, private residencies. This attacks have produced various casualties and dozens of civilians injured.
 - b.2 The continual closing of the Manuel Enrique Araujo Alameda since three years (see map). This is the main artery between San Salvador and Nueva San Salvador.
 - b.3 Reduction or failure of investment in some surrounding areas. For example, 80 percent of the nearby shopping mall, "Feria Rosa", has not been even been occupied yet.

6) Presidente Theater and parking space.

Designed for 1200 spectators. The theater is running into a fast obsolescence, the cinema facilities are hardly used and the parking space is highly under-utilized except for sporadic events. Current status: the theater and facilities are under increased pressure to be donated to the Direccion de Artes.

7) Torre Democracia.

A 20 floor building with 10000 m2 of built space valued at 60,000,000 colones. It was overtaken by the Nationalized Bank System, as result of the developers' failure to sell the building on the market. Its costs were a little lower than those of similar public buildings, however, its potential operational cost would be enormous since the building has to operate completely with air conditioning.

Current status: The building needs to be divested by the bank the bottom price estimated for sale is 80,000,000 colones. This

APPENDIX 5 A

Assume that the typical plot size in an urban area is 75 square meters or less. The beneficiaries of this program would pay an approximate quota of 40 to 60 colones monthly (7.5 dollars), as defined as the ceiling by the VMV. This figure is based in the amount that persons of low income (around 500 colones monthly) would be able to afford. Under the current 15% inflation and interest rates of 21%, this would mean that in a period of 15 years an individual would end up paying 4500 colones NPV (563 dollars NPV). This sum by the area of the typical plot would provide the ceiling to the price of land which could be available. This ceiling is around 60 colones V2. Since prices, at least in the Metropolitan Area of San Salvador (AMSS), are above this range (the price of land in the city ranges from 150 colones up to 1000 colones-- 18 dollars to 130 dollars) per V2. If the ceiling is maintained most publicly held land disposed of in urban areas require to be subsidy.

APPENDIX 5B

The Inventory of DCC shows a value for the portfolio of 453 million colones plus buildings in the process of construction valued at 843 millions. Adding a total of 1296 million colones for the total real property portfolio. This patrimony item is segregated from the national budget.

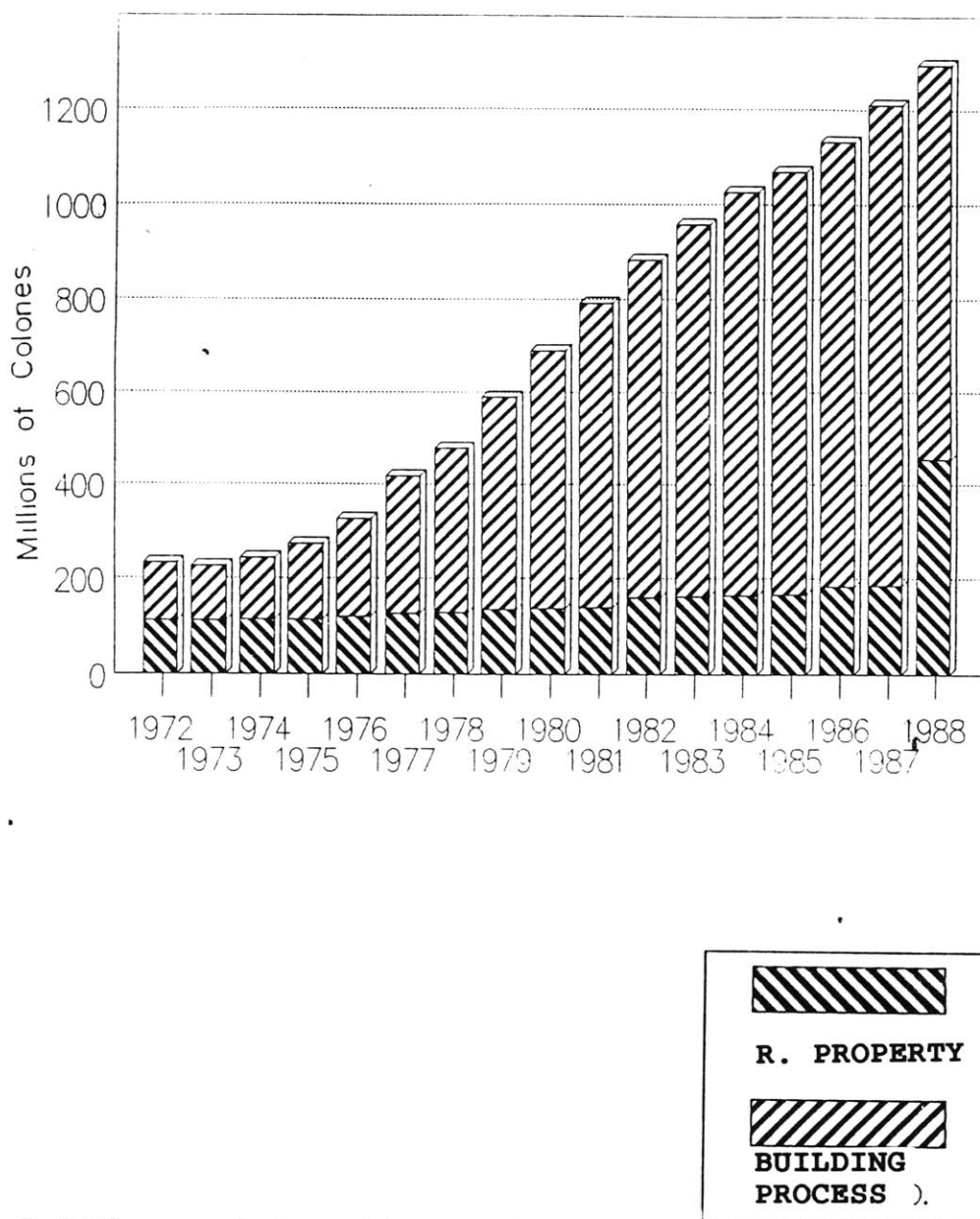


TABLE 5.1 (Source information gathered at the DCC reports from 1972-1988, for methodology see, the different data was put into table)

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ANNEX 6.1

FIELD WORK

Interviews with the next persons:

Dr. Ardito Harberger, economic consultant for the GOES.
Ing. Mauricio Stubig Minister of Public Works, El Salvador
Arq. Roberto Paredes, Vice Minister of Housing.
Lic. Ernesto Altschul, Vice Minister of Planning.
Dr. Pedro Arriagada, Executive Director of DEES , FUSADES
Lic. Hector Vidal, Head of DEES, Privatization Commission.
Arq. Gabriel Riesco, OAS delegate, Ministry of Planning.
Lic. Jose Marques, World Bank, Consultant for FUSADES
Arq. Leon Sol, OPAMSS
Lic. Mario Radelli, President of CORSAIN.
Lic. José Angel Quiroz, ViceMinister of Hacienda.
Lic. Manuel Alvarado Cano, Minister of Hacienda.
Mr. Sanabria, Director of the National Budget Direction.
Mr. Oscar Novoa, director of the Central Accounting Direction.
Ing. James Stephenson, USAID, private sector.

- * The National Budget Direction, that executes the valuations of all the real property assets, the government owns, leases or of the potential candidates. It values market conditions.
- * The Central Accounting Direction, is the institution part of the Ministry of Hacienda.
- * Fundacion Salvadorena de Desarrollo .