

**DRAFT**

Privatisation and Competition in the Telecommunications Industry – A case study of Mauritius.

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Abstract

The case of Mauritius illustrates that privatisation is generally conceived as a thorough government policy. However the results can be very different from the expectations. The inherent characteristics make the experience fairly unique. A framework adopted by Ofel is adopted to assess the feasibility of competition in the telecommunications industry in the island. A conceptual model is then provided.

## List of Acronyms

BNP	Banque Nationale de Paris
BOO	Build Own Operate
BOOT	Build Own Operate and Transfer
BOT	Build Operate Transfer
CIBC	Canadian Imperial Bank of Commerce
FT	France Telecom
GII	Global Information Infrastructure
GoM	Government of Mauritius
HDI	Human Development Index
ICTA	Information, Communication and Telecommunications Authority
IPO	Initial Public Offer
MLC	Mauritius Labour Congress
MT	Mauritius Telecom
MTS	Mauritius Telecommunications Services
OTS	Overseas Telecommunications Services
OTSEA	Overseas Telecommunications Service Association
PWPC	Privatisation and Workers' Participation Commission
SADC	Southern African Development Community
SATCC	Southern Africa Transport and Communications Commission
SDH	Synchronous Digital Hierarchy
TDM	Time Division Multiplexing
TSA	Telecommunications Service Association
TWA	Telecommunications Workers Association

## **1.1 Introduction**

The aim of the paper is to gain an appreciation of the Mauritian experience of privatisation with particular reference to the telecommunications industry. The country's specificities have significant policy implications and the small-island characteristics create the need to reassess the notion of competition and liberalisation of telecommunications services. The first section of the paper offers an overview of the Mauritian economy, the small-island characteristics and general privatisation experience. Section II shows a critical analysis of the privatisation of the telecommunications industry including the disparity between the intended motives behind privatisation and the actual effects, the weaknesses of the process and some important observations. In section III, the likelihood of competition in the telecommunications sector in Mauritius is reassessed drawing from general trends in the industry.

## **1.2 Methodology**

This paper is a case study and it relies on several data sources that converge in a triangulating fashion that constitutes an appropriate method of researching a contemporary phenomenon (Yin 1994). The main sources of evidence are documentation – policy documents, reports, legal documents, archival sources including parliamentary debates -, press articles and elite interview. Amongst the interviewees were government officials closely involved with the privatisation process and the telecommunications dossier, directors of current telecommunications companies, several stakeholders, trade unionists and staff members of the regulatory body. The paper is divided into three distinct parts. An overview of the Mauritian experience is presented followed by an appreciation of small-island characteristics that are revisited in part III where competition is analysed. Section II of the paper outlines the privatisation experience and the process.

## **1.3 Socio-economic profile of Mauritius**

Mauritius has a population of over 1.2 million people. It gained independence from Britain in 1968. Until early 1980s, Mauritius has remained a monocrop country with sugar as its main source of revenue. From 1976 to 1983, the rate of growth stagnated at 2.6% p.a. with worsening public sector deficits and balance of payments position.

The country experienced devaluation in 1979 and 1981. From 1983 to 1988, the situation improved following the adoption of the Stabilisation and Structural Adjustment Programme (SAP). Mauritius diversified its economy with the emergence of a manufacturing sector (Export Processing Zone). Other important pillars of the economy are tourism and offshore banking. Mauritius is often quoted as a success story in the realm of economic development and enjoys a higher standard of living than most Sub-Saharan countries.

**Table 1 Mauritius in figures**

Human Development Index (HDI rank) 2000	67
Life expectancy Index (2000)	0.77
Adult literacy (2000)	84.5%
GDP per capita (PPP \$) 2000	\$ 10017
Unemployment rate (2001)	9.2 %
Savings rate (2002)	26.3%
Investment by private sector (2002)	33.7 % of Gross Domestic Capital Formation
Public Sector Investment (2002)	63.7% of Gross Domestic Capital Formation
Rate of growth of economy (2002)	4.6%
Import of goods and services as a % of GDP (2000)	67%
Export of goods and services as a % of GDP (2000)	64%
Terms of trade (1980 = 100) in 2000	97
Annual Change in Consumer Price Index 1999-2000	4.2%

*Source: Central Statistics Office and UNDP*

PSEs have accounted for about 13% of GDP in recent years. The contribution of PSEs to GDP increased from around 10% in the early 1980s to about 14% in 1986-88 before declining slightly in recent years.

The share of the entire public sector, i.e. local and central government services combined in the GDP is around 24%. This is higher than the ceiling of 20% generally recommended for developing countries. PSEs account for 23% of gross domestic investment.

As regards efficiency, preliminary estimates suggest that labour productivity (measured by output per worker) in the private sector is on average higher than in the public sector. These measures can be challenged. Besides, the telecommunications

industry cannot be compared with the other public utilities facing financial difficulties.

#### **1.4 Small Island Characteristics**

The Commonwealth uses a threshold of 1.5 million population to define a small state. However a few bigger states sharing smallness characteristics are sometimes included (Jamaica, Lesotho, Namibia and Papua New Guinea) in the definition. The major economic implications of small size are as follows:

- **Remoteness and Insularity.** 34 out of the 45 small states are islands and are located far from major markets. Isolation also implies that small states find it difficult to compensate for the drawbacks of limited size and small domestic markets. The nature of telecommunications services is such that limited market size constitutes a severe limitation on the growth of the industry. “Limited market size (...) often results in a lack of competition; in some instances the size of the market can only support a single producer. As a result, the economies of small states do not benefit from the effects of competition on improving efficiency, lowering costs and spurring innovation.” (World Bank 2000 p.6).

- **Susceptibility to natural disasters.** Most such states are located in areas where there are extreme climatic conditions as well as natural disasters.
- **Limited Institutional Capacity.** The fixed costs associated with the provision of public services are fairly high. Such countries are also characterised by few specialists trained or retained. There is a lack of training leading to shortage of management skills, low levels of entrepreneurship, timid decision-making and routine dependence. In bilateral and other negotiations, the uneven balance of power significantly affects the outcomes.
- **Limited Diversification.** Many small states have very narrow resource base and are characterised by limited diversification.
- **Openness.** The economies are highly dependent on external trade and foreign investment. Openness can be extremely beneficial but it also leaves the countries vulnerable to changes in external conditions. Openness also entails that small countries have a larger stake in a stable, rule-based, world trade environment than their share of world trade would indicate.

- Access to external capital. Access to capital is crucial for small states. However, there is evidence to show that private markets tend to associate small states with higher risks.

The small states characteristics intuitively suggest that small states will be more vulnerable – greater exposure to exogenous shocks over which the affected country has little control and relatively low resilience to withstand and recover from these shocks- than their bigger counterparts.

Mauritius is referred to as a mini state. A mini state is defined as:

“one whose exposure to foreign trade is so important that economic events are largely beyond its control”. (Lamusse 2001 p.11)

The foreign sector is dominant and most of the production of the economy is geared for exports. The domestic sector is “a mere appendix of the export activities, largely dependent on them and cannot be planned exogenously” (Lamusse 2001 p.12).

There are two distinct aspects that are relevant in the economic characterisation of smallness:

1. International Aspect of smallness implying that the country is dependent on international trade.
2. The Techno-economic aspect of smallness – which is related to scale factor.

It is emphasised that overall Mauritius has been able to surmount several of the small-island constraints. However both these aspects are important in the telecommunications industry. Firstly, potential bidders will in most likelihood be foreign companies as no local company is engaged in the telecommunications business per se, though there are companies that provide certain value added services. The techno-economic aspect implies that there are limits to the absolute amount of profits that can be earned with the limited size of the market. The latter will be revisited in Section III when assessing the likelihood of competition.

## **2.1 The Privatisation Drive in Context**

Privatisation emerged as part of government policy. Government policies were to focus on increasing the ratio of private investment to capital formation from 65% to 80% in the medium-term. The plan was termed as ‘The New synergy’ and its main intended features were:

- i. a larger and yet more dynamic private sector
- ii. a public sector that concentrates on the role of the state as a guardian rather than as a direct producer of goods and services.
- iii. more democratised ownership
- iv. greater workers' participation in their enterprises
- v. more competitive market structure
- vi. sound regulatory and legal framework and
- vii. more direct participation of unions in productive activities and in enhancing productivity.

For the purpose of the White Paper, privatisation is defined as

“the process of transferring to the private sector activities which are being carried out by the public sector, with a view to improving efficiency, to raising the standard of living of the population and the quality of life, and to promote workers' participation and democratisation of ownership” (Government of Mauritius 1997 p33).

## **2.2 Extent of privatisation**

Privatisation has been fragmented in the country. In the energy and sugar sector, the creation of the State Investment Corporation enabled the allocation of shares of the Trust to small planters and workers amounting to 20% of the equity of milling companies (Parliament Archives 2000c). Representatives of workers/planters have seats on the Board of Directors of the 14 milling companies with about 13000 planters and 214,000 workers are involved.

Airport: The GOM signed an agreement with BAA (British Airports Authority) to benefit from the use of private sector management practices in the operation of the public service. The enterprise has remained under state ownership.

The objective of selling part of the shareholding of the State Bank to NEDBANK was to benefit from the international exposure of the partner. The partnership venture led to other joint ventures in Madagascar, Mozambique and possibly Tanzania.

Regarding the Central Water Authority (CWA), the Consortium Suez Lyonnaise des Eaux/Vivendi has been awarded a management contract. After six months, the original plan was to enter into a strategic partnership with the CWA as a concession

agreement under the Concession Projects Act 1997 that has now been repealed. The dossier was frozen.

The electricity sector had also been identified as a potential candidate for privatisation.

The Postal Services are also on the list for future privatisation. The Cabinet had already approved the creation of an independent regulatory body in view of the future privatisation. The regulatory body would be in charge of the running of postal services, courier services as well as auxiliary activities and the imposition of appropriate penalties. A second bill 'Post Office Bill' would be presented later this year to transfer the postal services to the a government-owned company Mauritius Ports Ltd (Le Mauricien September 23, 2002).

The state enterprises have been approached in a selective manner with a series of separate innovations. Some have been incorporated, some partially divested and a wide range of municipal services have been contracted out or commercialised by some municipalities.

The various methods of privatisation envisaged by the government in the White Paper had been divided in 3 main categories:

- divestiture of state assets;
- public enterprise reform under Government ownership; and
- involvement of the private sector in the supply of public goods and services.

Divestiture of state assets encompasses public flotation, private trade sale of all or part of the Government shareholding or management/employee buy-out. There are three stages prior to divestiture. The first step is generally commercialisation, the second is corporatisation and the third involves operational restructuring to establish the enterprise as commercially viable. The privatisation of the telecommunications industry in Mauritius followed that sequence except that there were not any major operational restructuring prior to selling of the shares.

When divestiture is not possible, a reform programme with a systemic sequence. A diagnostic review is carried out first followed by an enterprise restructuring phase whereby a performance contract between government and the enterprise management is reached.

Involvement of the private sector in the supply of goods and services can be achieved in a number of ways including contracting out, management contract, leasing arrangements and Private finance for Public Infrastructure (BOO, BOT, BOOT).

In the context, the white paper mentioned the creation of a Privatisation and Workers' Participation Commission (PWPC). Its main purpose was to evaluate the various privatisation proposals on a case-by-case basis. It was supposed to operate within a framework of guidelines formulated by government. However to date, this has not been created and as in the case of telecommunications, a committee within the Ministry of Finance was created to administer the privatisation process.

Privatisation has been on the agenda of the government since early eighties. It can be inferred that the IMF-World Bank pressure throughout 1970s and 1980s laid the foundation for privatisation. The need to reduce budget deficits has been a key driver of privatisation in Mauritius in accordance with the structural adjustment package of the World Bank. Thus, privatisation was espoused as an 'ideology'. (Government of Mauritius 1997<sup>1</sup>)

Evidence of privatisation as part of a strategy emerged more clearly in a document published in 1995 (World Bank Report on Mauritius – Mauritius: Country Economic Memorandum – Sharpening the Competitive Edge).

“ The public sector can achieve further efficiency gains through an accelerated parastatal divestiture program. While privatisation is being pursued as a means of achieving the broader economic goals of improved resource allocation, healthier public finance and increased domestic savings, a clear policy is not in place” Government of Mauritius 1997 p. 10 (white paper on privatisation)

The term “Mauritius Incorporated” was coined in the Budget Speech shortly after the publication of the report. (Government of Mauritius 1995).

“ There is the need to further liberalise our economy in line with our commitments to the WTO so as to facilitate its integration within the global economic and trade systems.” Budget Speech 1997 p 4

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<sup>1</sup> This policy document was compiled after consultations with several stakeholders including unions, Mauritius Labour Congress.

“ Early policy action will need to be taken in various areas for creating a new synergy as we approach the next millennium. Our focus will be on enhancing competitive market structures, speeding up the privatisation programmes, ensuring greater workers’ participation and accelerating reforms in the civil service and the parastatal bodies. ” Budget Speech 1997, p.5

The budget made landmark provisions from extra budgetary resources for giving additional boost to the socio-economic development. The special provisions were expected to be met from the approximate net proceeds of Rs 2 billion from the sale of Government shares in the Overseas Telecommunication Services Ltd. For the sake of transparency, the Government of Mauritius (GoM) created a Privatisation Fund, to which the net proceeds would be credited (The Privatisation Fund – Revenue and Expenditure – Act 1999). The Fund would be managed by the Treasury and audited by the Director of Audit. A separate Bill would be presented in the National Assembly to specify the companies whose shares will be offered for sale, the estimated proceeds from the sale, as well as the utilisation of the proceeds thereof. In this context, a draft Infrastructure Development ( BOT projects) Bill<sup>2</sup> was announced along with the White Paper on Privatisation and Workers’ Participation.

### **2.3 Telecommunications Restructuring**

As in most countries, the telecommunications sector was fully owned by the government and run under the Department of Telecommunications. In May 1988, a decision was taken to separate the functions of regulation and operation in telecommunications. The legal framework was provided for by the Telecommunications Act 1988 which also allowed for the creation of a Telecommunication Authority (Ministry of Telecommunications and Information Technology 1997a).

Privatisation was viewed as an essential ingredient in reaching the overall telecommunications policy of the country. The specific policy measures:

- a) New Legislation – repealing of Telecommunications Act 1988
- b) A new regulatory body

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<sup>2</sup> This Bill did not materialise.

- c) Transformation of government's primary role to being a policy maker as opposed to being the provider of services.
- d) Progressive Divestment by Government of its equity shares in Mauritius Telecom to investors
- e) The gradual introduction of competition and liberalisation of the sector.

The undertaking of the Government was transferred to Mauritius Telecommunications Services (MTS) Ltd. The company changed its name to Mauritius Telecom (MT) following a merger of the domestic and international services previously provided by Overseas Telecommunications Services Ltd (OTS). Despite the change in status of the industry, the government was indirectly involved in the operations of the industry through its majority ownership in MT.

#### **2.4 Present state of the Telecommunications Industry**

Mauritius Telecom now has 240,000 connected direct lines which equate to 22 lines per 100 inhabitants. In 1998, in SADC the penetration of personal computers was 1.97 per 100 inhabitants on average and the tele-density was 5 fixed telephone lines per 100 inhabitants whereas the world average stood at 6.43 per 100 inhabitants and 14.26 per 100 inhabitants respectively.

The digitalisation of the network has been characterised by state-of-the-art switching systems, high capacity microwave and optical fibre cable systems supported by Synchronous Digital Hierarchy (SDH) backbone for bandwidth regulation. The island-wide data transmission network, Mauridata, is based on the X.25 protocol with 600 access ports and X.75 links to France.

**Table 2 Basic Telephone Indicators**

	1996	1997	1999 <sup>3</sup>
<b>Basic Telephone Service</b>			
Main telephone lines	165,085	205,332	250,691
Unmet demand	41,141	27,299	27,184
Public Payphones	1,331	1,607	2643

<sup>3</sup> More recent statistics are not available except for the following. The main telephone lines and main telephone lines per 100 inhabitants in 2000 are 280,885 and 23.7 respectively.

<b>Data Communication</b>			
Packet Switch Subscribers	337	466	666
ISDN Subscribers	36	88	385
Leased Circuit Subscribers	645	689	867
<b>Other key Indicators</b>			
Main Telephone lines per 100 inhabitants	15	18	20
Faults per 100 main lines	78.24	62.7	55
Main telephone lines per employee	96	111	138

*Source: Mauritius Telecom*

**Table 3 Current Telecommunications Operators**

<b>OPERATORS</b>	<b>SERVICES OFFERED</b>
Mauritius Telecom (MT)	Basic Telephone including International Access; Payphones and Phonecards; Telex, X25: Data & Text; Internet
Cellplus Mobile Communications Ltd. (subsidiary of MT)	Cellular Mobile (GSM)
Teleservices (Joint Venture: MT & Singapore Telecom International)	Paging
Emtel Ltd.	Cellular Mobile (TACS)
Telecom Plus <sup>4</sup>	Internet services
Paging Services Ltd.	Paging

**Table 4 Growth of Network Users**

	<b>March 1995</b>	<b>October 1997</b>	<b>2000</b>	<b>2001</b>
Cellular Mobile Subscribers	10,000	37,000	179,452	299,523
Internet Subscribers	Insignificant	5300	86,740	157,748
Pagers	5,500	7,314	-	-

<sup>4</sup> Mauritius Telecom entered in a partnership with France Telecom in February 1996 with the aim of providing VAS that complement the development of basic network services.

At present MT has a monopoly over the international gateway, basic telephone, text, data and internet services to date despite competition being envisaged in the near future. Value added services include recent introduction of Tollfree 800, Itemised Billing, Call Barring, Call Forwarding and Call Waiting. At present competition exists in the cellular market and paging market segments only with the prevalence of private operators Emtel Ltd providing mobile telephony services and Paging Services Ltd. Emtel Ltd came into business in 1989 as the first mobile telephony provider with a Telephone Access Communications System (TACS). Cellplus Mobile Communications Ltd, a subsidiary of MT obtained a licence to operate a Global System Mobile (GSM) cellular mobile system in September 1996 with exclusivity to use GSM technology up to 1999. Paging Services Ltd started operation in 1988 and Teleservices ( a joint venture of MT and Singapore Telecom International) entered the market in 1991. The two private operators possess their own network and are interconnected to the MT network on the basis of a formal agreement.

The fully digital switching network comprises eight main exchanges, 45 remote exchanges serving the rural areas, and one exchange for Rodrigues. The first generation of digital exchanges installed in 1976 were replaced less than 10 years later by third generation Alcatel E10B/OCB283 exchanges. All exchanges are capable of supporting 100% DTMF (Dual Tone Multi Frequency) dialling. SDH technology, fibre optic cable systems and digital two-way radio are used to link all exchanges. MT has direct links with 19 countries and direct dialling access to another international destinations. A 15 metre Standard A station works with the Intelsat 60 degree satellite providing services to Australia, Belgium, Hong Kong, Italy, Japan, Kenya, Madagascar, Seychelles, Singapore, South Africa, Switzerland, Taiwan and the UK. International as well as global roaming traffic transit through an International Gateway that is connected to the world via International Satellite Communications Organization (INTELSAT)<sup>5</sup>. The networks are fully digitalised with a digital narrowband technology platform supporting the backbone network. The telecommunications operation is conducted over transmission links with a maximum switched-bandwidth of 64 kilobits per second per channel. The bearers used are

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<sup>5</sup> INTELSAT is a provider of fixed satellite communications services. It supplies the facility for the establishment of fixed transmission links between countries for the operation of telephone, facsimile, computer-internetworking, music and services. It is an international organisation with 200 members.

limited to microwave and optical fibre cables transporting information using the Time Division Multiplexing (TDM) techniques.

## **2.5 Mauritian Telecommunications Industry in an international context**

Mauritius belongs to two organisations that deal with policies on telecommunications namely the International Telecommunications Union (ITU) and Southern Africa Transport and Commission (SATCC). SATCC was established in July 1981 as the ordination Conference (SADCC). It was established under the terms of the Lusaka Declaration on April 1, 1980. The supreme body of the SATCC is the Committee of Ministers comprising one member from each SADC State, generally being the Minister responsible for transport and communications. The Committee of Ministers is advised by the Co-ordinating Committee, usually made up of Permanent Secretaries or senior government officials from the same ministries of transport and communications.

The SADC Protocol on Transport and Communications adopted by member states in August 1996 provides guidelines for governments to adopt a policy role and for operation to be pursued by private investors under the supervision of an independent regulatory institution. Mauritius is also a signatory in two organisations that provide satellite transmission facilities – INTELSAT and INMARSAT<sup>6</sup>

“ The globalisation of economies resulting from the liberalisation of trade and services under the auspices of the World Trade Organisation (WTO) is further pressurising governments worldwide to open their markets to competition. Mauritius took commitment on February 15, 1997 at the WTO Working Group on basic telecommunications services to open up the telecommunications sector to competition and to end all monopoly and exclusive rights in domestic and international services by the year 2004” Ministry of Telecommunications and Information Technology 1997a p.15).

## **2.6 Telecommunications Policy**

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<sup>6</sup> INMARSAT is a provider of world-wide mobile satellite communications. It specialises in the provision of maritime, aeronautical and land-mobile satellite services, supporting particularly telephone, facsimile and computer-internetworking. It is funded by members from about 79 countries.

Unlike other African states, Mauritius has achieved a high penetration rate and the telecommunications policy is an integral part of the overall development of the economy by creating another important pillar. In Mauritius, the telecommunications policy is an extension of that espoused by WTO and the compelling necessity to become an “information economy”. It rests on the growth and sustainability of the national info-communication sector. The key drivers of an information-based economy are:

1. the development of the local information sector
2. the establishment of a National Information Infrastructure (NII)
3. the orientation of info-communication services to users.

Information services in Mauritius can be categorised under telecommunications services and broadcasting services. They are separate networks with the only area of convergence being the international telecommunications network, where common bearers are used for the transport of the two sets of services.

The concept of NII has been established to create an extensive diffusion of multimedia applications and galvanise the flow of information, in support of inter-country trade. The telecommunications industry has embraced the philosophy of NII to design its policies. The concept originated following the concept of Global Information Infrastructure (GII) in 1994. The concept was adopted by the G7 Ministerial Conference held in Brussels in February 1995. The eight principles guiding its realisation are:

- a. providing open access to networks
- b. Ensuring universal provision of, and access to, services.
- c. Encouraging private investment
- d. Promoting diversity of content
- e. Promoting equality of opportunity
- f. Promoting dynamic competition
- g. Defining an adaptable regulatory framework
- h. Recognising the necessity of world-wide cooperation with particular attention to less developed countries (Green Paper 1997 p. 20)

## **2.7 Mode of privatisation preferred**

The “participation model of privatisation” is used to describe the option whereby firms are sold for cash but the state retains a proportionate share of ownership. This has been popular in transitional economies mainly (Bennett *et al.* 2000). It is also analogous to the ‘golden share’ approach adopted by Britain in the privatisation of both water and telecommunications industry. The Strategic partner is entrusted with certain rights relating to management and control of MT.

## **2.8 Privatisation process**

The privatisation can be viewed at two different levels. The first stage involved the selection of a consultant followed by the actual selection of potential buyers. The selection of a consultant proved to assist the GOM on the privatisation proved fairly controversial and cannot be discarded.

In June 1995 the Cabinet decided to appoint a consultant to advise on the modalities of listing MT on the Stock Exchange Market. The question that arises is whether the sequencing matter

Option 1: Stock Exchange listing first followed by privatisation.

Option 2: Privatisation first and then Stock Exchange listing.

In August 1995, MT decided to appoint a consultant to advise on an Action Plan prior to the listing exercise emanating from the Cabinet decision. Tenders were soon launched and at the closing date, ten offers were received. The Central Tender Board then affirmed that under current legislation, it was not entitled to evaluate the bids on behalf of MT. The Finance Minister then took the necessary steps to bring the necessary amendments to the schedule of the CTB Act. The general elections then followed, jeopardising the exercise.

In September 1997, representatives of MT and GOM decided that it was in the best interest of all stakeholders if a strategic partner was chosen before proceeding with the Initial Public Offer (IPO). The reasoning behind this decision is however unknown and it has not been satisfactorily demonstrated in what way the preferred option is superior.

In October 1997, MT launched a tender for the selection of a Financial Adviser to be responsible for the preparation. The bids were evaluated by the Tender Committee of MT in December 1997 – January 1998. In July 1998 the Cabinet requested the Financial Secretary to scrutinise the procedures followed in the tendering exercise.

The committee pointed out that the evaluation had not been done in accordance with the criteria set which involved a point system. Hence the process was halted. The services of two Public Procurement specialists were retained to advise into the matter. They suggested that GOM should be responsible for the tender and not MT, as MT would be in a situation of conflict at the time of negotiation with the prospective strategic partner equity partners.

CIBC – the 5% (about Rs 350m) success fee was severely criticised. Thereafter the success fee was in fact 1.7%. The Cabinet took note of the decision of the Central Tender Board to award to the Canadian Imperial Bank of Commerce (CIBC) the contract to act as a financial adviser to Government. The minimum technical criteria for the selection was:

- i. relevant experience for the assignment
- ii. quality of the methodology proposed and time frame; and
- iii. qualifications of key staff proposed

The Opposition objected to the very fact that an Investment Bank was chosen in lieu of a specialised consultant, for instance the Corporate Finance Services Department of the IFC or the World Bank. Unionists believed that the privatisation was done in utmost secrecy.

The final offers from the three bidders for 40% of the shares of MT were as follows: France Telecom was the highest at US\$ 261 m, Vivendi with US\$255 and Portugal Telecom with US\$220. The bids were made on the basis of the transaction Documents. The shareholders agreement will guide the way MT, the strategic partner and Government work together. The shareholders agreement specifies a Board of Directors on which the Government will hold five seats, including those of chairman and chief executive and the strategic partner four members. Day to day operations will be the prerogative of the operating committee that is responsible in implementing the annual business plan. The shareholders agreement also imposes restrictions on the ability of the strategic partner to sell on its shares, as Government wishes to have a long-term partner at MT and requires the strategic partner to co-operate with Government in the future flotation of the company on the Stock Exchange.

The last of the transaction documents is the services agreement. The strategic partner was expected to contribute in terms of expertise, new technology, training, investment and international links.

The services provided by the partner are to be spelled out in the annual business plan and needs to be approved by the Board. The value of services provided could be up to 5% of MT's gross revenues.

The tender process was transparent and none of the bidders raised any objections regarding the same. The selection of government advisers was approved by the Central Tender Board. The marketing of MT involved contacting several potential bidders as well as advertising in the media. Pre-qualified bidders were provided with all the relevant information on the company and were given the opportunity to carry out 'due diligence' visits twice before the preliminary bid and once before the final bid. All bidders had access to the same information.

Portugal Telecom was bidding alongside a big South African operator, MTN. They withdrew two days before the closing of the bidding process. The reasons behind the withdrawal are unknown. Later the main reason in the public domain was that the Board of MTN opposed the venture hence leaving Portugal Telecom with no choice other than withdrawing its application.

The privatisation of MT was to be effected in two phases. In phase I, 40% of the shares will be sold to the strategic partner as well as 1% to employees. Phase II encompassed a move to IPO. To date, the employees have been unable to buy any shares and there are no concrete plans to concretise the IPO.

This tendering process leads to interesting observations:

Negotiations started with France Telecom<sup>7</sup>. Initially MT and its advisers, Ministry of Finance and its adviser CIBC would be involved in the negotiation process with regular reports to parliament.

Before privatisation, the shareholding structure of Mauritius Telecom was as follows:

**Table 5 Structure of MT**

	%
Government	51.95
SIFCOR (the warehousing company)	22.50
NPF (National Pension Fund)	06.55
State Commercial Bank Ltd	19.00

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<sup>7</sup> Negotiations with Vivendi could only start in the event there is no agreement reached with the most preferred bidder.

After the disposal of shares, the shareholding structure were meant to be as follows:

**Table 6 Intended Shareholding Structure**

	%
Government	10.00
State Bank of Mauritius Ltd	19.00
Public Sector Institutions (Including NPF)	30.00
Employees of MT	01.00
Strategic Investor	40.00

*Source: Parliament Archives ( 2000 a)*

However in the aftermath of privatisation, the share distribution stands as follows:

**Table 7 Share structure of MT today**

Shareholder	Percentage of issued share capital held (%)
France Telecom	40.00
Government of Mauritius	34.45
National Pension Fund	6.55
State Commercial Bank of Mauritius	19.00

The GoM *per se* owns about 5% of the issued share capital of the State Commercial Bank Ltd while the National Pension Fund owns about 15%. Moreover, major shareholders include several government owned institutions and bodies ([www.sbmonline.com/ann2001/sharerel.htm](http://www.sbmonline.com/ann2001/sharerel.htm)).

The State Commercial Bank is a private company which has signed a strategic agreement with a South African strategic partner – NEDCOR. However the Government insists that because it controls the Board of the State Commercial Bank Ltd., it can be taken to be part of the public sector. There was a Cabinet decision to allow Government’s shareholding in MT to fall below 50%<sup>8</sup>.

There were concerns that selling 40% of the stake to a foreign partner would represent a change of control. The bids of Vivendi, the second bidder was only Rs 200m short on the one proposed by France Telecom. The decision to choose a final partner then had to be taken on other than financial grounds. France Telecom got the upper hand based on the following:

1. The superior technology

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<sup>8</sup> France Telecom had just bought Orange. One of the conditions was that French government keeps at least 50%.

## 2. The Mauritian Government remains the majority shareholder.

At that time, the financial viability of France Telecom had been identified as a problem.

It was clear from several policy documents that strategic alliances was a favoured mode of privatisation.

“ Government will opt for strategic alliances wherever possible so as to facilitate the transfer of state of the art technology and to enhance the efficiency and effectiveness of our public sector bodies so as to deliver better quality and cost-effective service to the nation.” Parliament Archives (2000b)

Before the negotiations of the sale of MT, the GOM had already committed expenditure amounting to Rs 7.7 billion to be financed by the proceeds from the sale of shares of MT. As at June 2000, Rs 1.9 billion had already been spent. The GOM also conceived a warehousing scheme that since July 2000, had resulted in interest liability amounting to Rs 500,000 daily (Parliament Archives 2000c).

At the end of September 2000, the new Government appointed a consultative committee – representatives of both Government and MT – to assess the deal. On October 13, 2000, the GOM gave a mandate to the negotiating committee to open negotiations with France telecom, the highest bidder. The negotiating committee was composed of the Financial Secretary, the Solicitor-General, the Permanent Secretary of the Ministry of Information Technology and Telecommunications, the Chairman and Chief Executive of MT. Those negotiations started on November 6, 2000 and were concluded in five days. The cabinet was convened on the following day and the closing agreement was signed immediately after.

The GOM will retain full control of the Board as long as GOM together with “state-controlled entities” own 30% or more of the shares.

The GOM would consider the advisability of disposing of all or part of its shares over the medium-term by way of private sales and/or by way of flotation on the Mauritius Stock Exchange.

Regarding procurement obligations of MT, the original services agreement gave France Telecom a guaranteed minimum in the provision of services and equipment to MT. In the final agreement, the procurement was decided to be with no guaranteed minimum but a first preference would be given to FT in case their rates are competitive.

At the time of concluding the contract, FT made a statement of intention about the possibility of creating more employment in the future.

The payment for the sale of the shares of MT amounted to US\$26 m (amounting to Rs 7.2 billion). The warehousing agreement would absorb Rs 2.4 billion and Rs 2.3 billion will have to be credited to the Privatisation Fund, in respect to projects agreed in 1999/2000. An amount of Rs3 billion has been earmarked in the 2000/2001 Capital Budget for financing development projects.

## **2.9 Views on Privatisation**

There has been mixed views about the necessity to privatise. On the one hand, interviewees argued that it was the only way forward for the telecommunications industry. Privatisation was merely a policy decision of the government. Those who advocated privatisation as an imperative choice also acknowledged the fact that the costs could have been reduced drastically.

Many interviewees believed that a strategic partner was not at all necessary for MT to become a major player in the region.

The union opposed privatisation for the following reasons:

1. In the first instance, any privatisation is opposed on ideological grounds. Experiences of privatisation in the world support the fact that the venture is always accompanied by cuts in the workforce. However eighteen months after privatisation, there has been no laying-off as it is believed that the government is still in control of 60% of the shares.
2. There were fears that the company would lose its social responsibility – universal agreement and low tariffs. It was anticipated that privatisation would necessarily be followed by tariff rebalancing whereby prices of domestic calls will rise and prices of international calls will fall<sup>9</sup>. Most people in the country are more concerned with national calls and a rise in the price will definitely make most Mauritians worse off.

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<sup>9</sup> Tariff rebalancing is the process whereby charges of calls are more closely related to the costs of providing the services. Consequently revenues from international calls will no longer be used to cross-subsidise local and national calls. This exercise has taken place in October 2002 but its implication is beyond the scope of this paper.

The union representatives – Telecommunications Service Association (TSA), The Mauritius Labour Congress (MLC), the Overseas Telecommunications Service Association (OTSEA) and the Telecommunication Workers Union - have recently made a public declaration requesting the departure of FT. The unionists are in favour of GOM buying back the shares that it disposed of in November 2000. The reasons for this move towards ‘renationalisation’ are:

1. There has been no significant contribution made FT since it became the strategic partner of MT in November 2000.
2. FT was meant to have assisted MT in gaining market share in Africa and nothing has happened to that effect.
3. According to one of the traded unionist, MT reaped profits amounting to Rs 1.5 billion in the previous year and without FT, the profits would have exceeded Rs. 2 billion.
4. At the conclusion of the deal, FT announced its intention to create about 600 jobs in the company. At present, it is stipulated that there are 200 extra workers in the company.
5. The financial difficulties that FT faces nowadays - the debts are around 70 billion euros and losses have amounted to 12 billion euros for the first half of the year (Le Mauricien October 2, 2002) – can have negative effects on MT in general.

The French Government owns 55.4% of the shares of FT. Despite its losses of over 12 billion euros, FT has recorded an increase of 13.6% in its operating revenues. This increase is mainly due to its subsidiary Orange operating in the mobile telephone services, the basic fixed telephony in France as well as the Internet group Wanadoo. In September 2002, FT announced the separation with the German mobile operator MobilCom in which FT owned 28.5% of the shares. The director general of the company has been replaced following the under performance of the company. FT is expected to present a disinvestments plan in due course. There are concerns in Mauritius about the possibility of FT disposing of its shares in MT. (Le Mauricien, September 23, 2002)

## **2.10 Privatisation – A Critical Appraisal**

In assessing the privatisation venture five main points are noted:

1. Eighteen months after the privatisation, there are no significant changes in the company. Most experiences of privatisation reveal major restructuring either before or after the conclusion of the deal. In this case several changes have happened within the company but none can be directly attributed to privatisation. There are currently four representatives of FT working at MT – two as per the shareholders agreement and at a later stage two more joined. The Deputy Chief Executive and Chief Operating Officer. They are generally responsible for general operational matters, network issues and development of the company as a whole. One is in charge of strategic management and the other one is a commercial director. The services of more FT employees are called upon as the need arises. None of the employees currently posted at MT was involved in the negotiations leading to the privatisation.

From the perspective of the regulator, privatisation has not led to any difference. Information Communication and Telecommunication Authority ICTA was involved in the issuing of a new licence with different terms and conditions. It is however suspected that there are many internal disagreements between MT and FT but by the time they need to negotiate with ICTA, they would have reached a consensus.

2. The White Paper on Privatisation and Workers' Participation outlined the concept and approach to the restructuring of the Mauritian economy. The main ingredients of such a policy are:
  - a. A larger and more dynamic private sector while the role of the state is restricted to that of a facilitator and regulator
  - b. Greater participation of workers in their enterprises
  - c. A more broad-based and democratic ownership, leading to higher standards of living for the population and
  - d. A good regulatory framework, with an effective regulatory mechanism ensuring a level-playing field.

With the privatisation of MT, at least to date, the workers and the public in general have not been able to buy any shares in the company.

3. One of the reasons advocated for privatisation is the inefficiency of the state run enterprises. In the case of MT, this is obviously not the case. Furthermore,

40% of the government shares have been bought by FT whose capital is mostly owned by the French government. The Ownership Model chosen is subject to criticisms. Several empirical works cited in Errunza and Mazumdar (2001) have demonstrated that private ownership is superior to public ownership. There is also enough evidence to suggest that the efficiency gains expected as a result of change in ownership are fairly small. If a public sector enterprise operated efficiently under government ownership, then the gains of privatisation are expected to be low. (Errunza & Mazumdar 2001). Unfortunately, there is not enough data to empirically investigate the case of MT.

France Telecom is a foreign company but it should be borne in mind that the French Government is the major shareholder of France Telecom as stated above, hence further weakening the premise that transfer of ownership to the private sector is a means to achieve efficiency.

The inefficient public sector argument cannot be held for the following reasons:

- a. The profits of MT over the past few years stand as follows:

**Table 8 MT profits**

	1996 (Rs)	1997(Rs)	1998 (Rs)	1999 (Rs)
Profit after taxation and before dividend	416,904	725,984	759,984	937,451

*Source: Mauritius Telecom website*

This contrasts with the losses made in the water and electricity sector.

The relationships among the different stakeholders – There are four major sets of actors each with a different agenda:

The GOM was looking to dispose of its shares and obtain the maximum proceeds in the set time to finance budget deficits.

4. The small island characteristic entails that there are more chances that in the event of privatisation, the strategic partner or outright buyer is more likely to be a foreign company. This has several implications on the macroeconomic variables of the country including the balance of payments.

5. Another important observation is that privatisation emerged elegantly as a policy of a government. However the pace of privatisation was affected by the mounting budget deficits. The privatisation that has been on the agenda for years took place within a few weeks after a change in administration. In addition, the anticipated proceeds from privatisation had already been earmarked and utilised, hence making the need to find finances even more pressing.

### **3.1 Competition**

This part of the paper evaluates whether it is realistic to expect competition to be instilled in the telecommunications sector in Mauritius.

Traditionally it was impossible to perceive competitive in so called natural monopoly situations (Mason and Valletti 2001; Armstrong 1997). However nowadays competition is beginning to be the norm and in the telecommunications industry, it has been made possible mainly due to technological advancement (Laffont and Tirole 2000; Ordober 2000). Competition finds its roots in the contestable theory literature and the merits are numerous (Ofel 1998; Lehr and Glassman 2001; IRG 2001; Acutt and Elliott 2001). Effective Competition can be defined as

“ the persistent absence of players with market power. In an effectively competitive market users are better off, because they are more likely to be provided a greater variety of products and/or services of lower price and higher quality than they could be provided in a non-competitive market” IRG 2001 p. 2

If competition becomes effective and established, subscribers will have a choice of local network, there would be different network technologies and the incumbent operator will become under pressure to reduce its local network costs, introduce innovative services and several attractive packages.

The threat of competition in developing countries has had an impact on incumbent monopolies. It has been shown that if liberalisation is imminent in the next three years, there is a strong statistical correlation between the threat of competition and the increasing rates of teledensity growth (Petrazzini 1996).

### **3.2 Ways of Introducing Competition**

Competition can take various forms, such as competition for outputs, inputs, franchises and outright takeovers.

It is useful to classify the telecommunications services in different categories and then assess where they lie on the competition continuum. The categories identified are: local fixed network operation, local mobile network operation<sup>10</sup>, long-distance (international) network operation and service provision over combinations of the above networks (Armstrong 1997). Regarding service provision over fixed networks, there are two ways in which competition can be achieved:

- i. An entrant can install new network and provided services directly. Each user should have a wire or a microwave link to the network.
- ii. The entrant can use the infrastructure of the incumbent to provide indirect access provision mainly for long-distance and international calls. Generally, subscribers connected to the incumbent network have to dial a number to get onto the network of the entrant.

### **3.3 Feasibility of Competition in Mauritius**

The telecommunications policies in Mauritius are based on the premise that competition will be prevalent. External conditions of potential competition are envisaged whereby firms from outside the market are anticipated to try to enter in the future hence influencing the choices by firms inside the market. There is a distinction between internal conditions of potential competition and external conditions of potential competition (Shepherd 1984). The former encompasses the extent of actual competition and monopoly among existing firms – non-existent in the fixed telephony.

The revised methodology for assessing the extent of competition is adopted as a framework in an attempt to assess the viability of competition in the fixed telephone market in Mauritius (OfTel 1998). OfTel uses a simple two- stage process:

#### Stage 1 Product Market Definition

##### Main Issues

- Demand-side substitution

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<sup>10</sup> There are two mobile telephone operators in Mauritius but the focus of this paper is competition on the local fixed network.

- Supply-side substitution
- Geographic Scope of the market

## Stage 2 Analysis of extent of Competition

### Main Issues

- Structure of Market
- Behaviour of firms
- Barriers of entry

It is noted that these two processes are not separate. Demand-side substitution considers the availability of alternatives to the subscribers. The concept of 'hypothetical monopolist' is based on whether the subscriber can switch without incurring any significant costs referred to as switching costs below.

Supply-side substitution focuses the ability of a firm to change its provision of services following a change in price.

The geographical scope of the market is defined in terms of the products or services as well as in terms of a particular geographic area.

In Stage 2, given the absence of a superior measure of the extent of competition, market share is often used as an indicator. However it is recognised that this measure only provides a partial picture and it is silent regarding the contestability of the market. It is important to obtain an idea of the existence of barriers to entry to understand the degree to which the actions of incumbents are affected by the threat of new entry. This simple equation shows the barriers to entry.

$$\mathbf{Rate\ of\ entry = a_0 + a_1\ Growth\ in\ industry + a_2\ Costs\ of\ operation + a_3\ Sunk\ cost + a_4\ excess\ capacity} \quad (1)$$

Sunk costs can be used as a proxy to assess the barriers to exit. The sunk costs would determine the ease with which the firm can exit the market. The extent of physical capital would depend on the forms of competition. The non-physical forms of sunk cost may be larger with the given technological state.

Cost of operation will determine the profitability of entering the market. It depends on the interconnection charges that will constitute the biggest cost, the final prices that the operators are able to charge depending on the prevailing regulation.

(Sunk costs of costs of operation are probably collinear but this is just a simplistic model to try and assess how realistic it is to assume the concretisation of competition).

Growth in industry refers to the prospects in growth in demand. It is assumed that external changes in technological development would lead to changes in the telecommunications industry. Growth in demand seems intuitively unlikely as it depends on a number of factors. Another important consideration in the telecommunications market is the existence of excess capacity in the market and the ease of access of such capacity.

$$\text{Growth in industry} = b_0 + b_1 \text{ switching costs} + b_2 \text{ difference in prices amongst competitors} + b_3 \text{ external factors} + b_4 \text{ penetration rate} + b_5 \text{ regulation} + b_6 \text{ other factors.} \quad (2)$$

Switching costs refer to the costs of changing operators. This obviously depends on the form of competition – whether the subscriber stays with the incumbent and dial a number to gain access to the competitor’s network, whether the subscriber actually needs to invest in physical equipment such as a box. It also depends on the time involved in shopping round several competitors. These costs must be a minimum so that subscribers are induced to switch operator. Armstrong (1998) refers to ‘costs of arranging contractual relationship with new operator’. Empirical studies in the electricity market have proved that switching costs are very important (Guilietti *et al.* 2000). The range of services offered by new entrants will also influence subscriber’s decision whether to switch. Another important consideration is whether the subscriber would be able to keep his number hence making number portability an important variable.

On analysing the UK market after over fifteen years of the liberalisation of the market, it can be inferred that in Mauritius, we can expect one firm to dominate the market given the limited domestic market. In a study on developing countries, it is emphasised that

“ In many cases, new entrants have had difficulties in taking any significant share of the market, let alone growing large enough to gain market power and become a serious threat to the incumbent” Petrazzini 1996 p. 3

Malaysia introduced competition in long-distance and international calls but none of the entrants could gain a significant market share.

The trend in other countries can be tentatively used to predict the case in Mauritius.

1. The size of the market is extremely limited. (saturation point in fixed telephony).
2. Competition has been really slow to pick up in UK despite a comparatively larger market. The following table shows the market shares of BT and Mercury in 1992/3 (Business and Residential)

The market shares of BT and Mercury in 1992/3 (Business and Residential)  
Percent

	BT	Mercury
(directly connected)		
Subscribers	98.7	0.5
Local Call minutes	95.6	3.0
National Calls minutes	89.2	10.5
International Call minutes	77.4	21.9

*Source:* Armstrong (1998)

Assuming a trend similar the UK experience in Mauritius, 0.5% of subscribers would mean 12500 subscribers<sup>11</sup>. The revenue approximated may not be enough to make the competitor's business viable *ceteris paribus* or in the absence of cross subsidisation. Consequently it may be hard to attract competitors. (other things to consider – Telecommunications Policy of the government – other details – e.g. equal access, switching costs etc).

Market Shares in December 1996 (Business and Residential)

Percent

	BT	Mercury	Cable	Others
Subscribers	90.6	1.0	7.5	0.9
Local call Minutes	86.1	2.4	9.8	1.7
National Calls Minutes	79.1	10.7	5.1	5.1
International Calls Minutes	57.9	15.6	5.1	21.4

*Source:* Armstrong (1998)

<sup>11</sup> Unfortunately there is no data available to calculate the revenue per subscriber. The latter would constitute an indication of the smallness of the market.

Market Shares in December 1996 (Residential)  
Percent

	BT	Mercury	Cable	Others
Subscribers	90.4	0.0	9.0	0.6
Local call Minutes	88.3	0.1	11.5	0.1
National Calls Minutes	88.3	5.0	6.4	0.3
International Calls Minutes	77.0	8.1	8.0	6.9

Armstrong argued that the technological features of local networks do not support the premise that local competition will involve more than two or three firms in the residential markets whereas the long-distance and international markets tend to be more competitive. (Armstrong 1997). In Mauritius because of the smallness of the country, in the recent tariff rebalancing exercise, there is no longer any distinction between local and national calls. The rationale behind this decision is that the cost of provision of a local call is not very different from that of a national call as a result of full digitalisation of networks. This elimination of national calls eliminates one potential competitive area that has been able to attract new entrants in countries that have liberalised their networks.

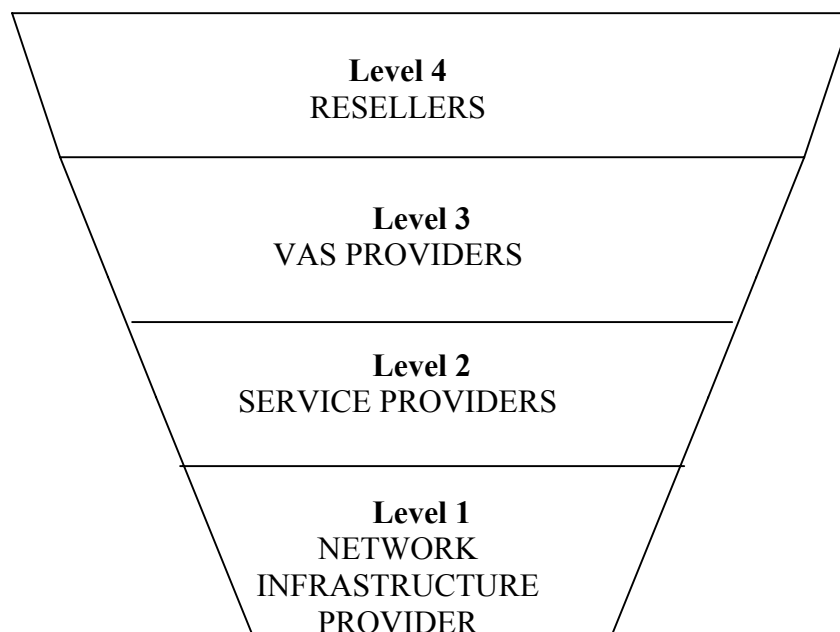
### 3.4 Implications of possible lack of competition

It is postulated that the government policy focused on competition in output is unlikely to reap the positive anticipated effects in Mauritius. Hence to benefit from the advantages of competition, other forms of competition need to be considered. Most utilities are granted licences for a specified period of time. These licences can be open to competitive bidding hence the competition is for a monopoly right. However this assumes the existence of several bidders or existence of entrepreneurs. The smallness of the island limits the scope for local entrepreneurs.

Outright takeover is another form of introducing competition as mentioned in Section 3.2. This relies to competition on the capital market. The necessary condition is to have a highly functional stock market. In the case of MT, it is not even listed on the Stock Exchange and also the Shareholder's Agreement (Ministry of Finance 2000) deters competition. If the GOM wishes to sell its shares, it needs to offer them to FT in the first place.

Competition in output market can be achieved using the same approach as mobile telephony in the UK whereby airtime providers cannot sell directly to the public. This is similar to the model proposed in Trinidad and Tobago (Baksh 2000).

Fig 1 Conceptual Model for Introducing Competition in Telecommunications in Mauritius



**Source: Baksh 2002**

The inverted pyramid shows that there will be more competition – hence more firms at the top than at the bottom. In this scenario, all the companies are to be listed on the stock exchange. As things stand, theoretically MT should remain the network infrastructure provider with the responsibility of maintaining the network. However it is not allowed to sell telecommunication services directly to the public. Initially there will be several new entrants at levels 2, 3 and 4 therefore constituting a level playing field. Barriers to entry will also be smaller at those levels.

#### **4. Conclusion**

An overview of the privatisation of the telecommunications industry in Mauritius has been presented. The small-island characteristics make the experience rather unique. The salient main points are that privatisation was a result of a short-term need to finance mounting budget deficits. The sequence of privatisation has far-reaching consequences that had been ignored. In the privatisation process, the role of the consultant is very important and complicates the privatisation process and raises certain governance issues. The actual results of privatisation have diverged significantly from the intended effects. In addition the experience shows that most of the theoretical justifications of privatisation were not present. The telecommunications policy of the government is based on the idea of competition as an emerging characteristic of the industry. The framework used to assess the extent of competition has been used to demonstrate that competition in the output market is not feasible in Mauritius due to the inherent characteristics of the country. A conceptual framework has been proposed instead.

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