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Privatization risks

PRIVATIZATION is currently passing through a critical phase of sell-off of large enterprises, raising legitimate concerns about divesting of profitable strategic national assets like Pakistan State Oil. Many see wholesale privatization, based on the concept that it is not the business of the state to be in business, as flawed for a developing economy with a weak private sector. Privatization is a particularly complex issue in the case of strategic assets like PSO, as pointed out by a planning expert in an article in this newspaper the other day. The company was formed by the merger of nationalized oil distribution firms and its assets created over decades have a replacement value at current prices which would be several times more than the book value. The transfer and control of these massive assets to a small group of foreign shareholders carry risks inherent in the nature of management. Two of the three serious bidders are groups from oil-producing countries. Petroleum policy has made oil marketing a lucrative business. Oil is globally a strategic commodity as demonstrated by the Iraq war, and more so for Pakistan, because oil accounts for a quarter of our import bill. The purchaser will import and market oil worth billions of dollars without any sizable investment and transfer of technology or creating any new production capacity and employment opportunity. Oil is the most important energy source that fuels economic growth and is also a sensitive consumer item.

The perceived risks in privatization emerge from enhanced global security concerns and a sales strategy that deprives the country of a reliable flow of revenues from profitable concerns giving much better returns than the rate at which the government has normally borrowed. Over the years the government has been burdened with a large portfolio of sick units, particularly Wapda and the KESC. This has meant heavy subsidies that have inflated budget deficits when in the post-nationalization period, taxes paid by taken-over units had doubled. In the existing situation, the domestic private sector does not have enough resources to compete in bids for big banks, oil companies and telecom agencies. Public sector units can only be sold to foreigners who may end up taking all the strategic national assets. As a consequence, the domestic private sector will be denied an even playing field. Even some of the most ardent advocates of privatization, therefore, differ on its timing, speed and sequence and also on the textbook approach adopted by policy-makers on the advice of multilateral donors. Some of these large enterprises being brought under the hammer dominate or control the market, even if all of them may not come under the definition of monopolies. It is argued that given the level of corporate social responsibility, consumers cannot be left at the mercy of cartels or monopolies. The public good and considerations of national security should be at the heart of the privatization move.

Similarly, if privatization proceeds too speedily, it tempts private investors to purchase the existing assets instead of creating new productive capacity. No wonder, the ill-conceived and badly-executed privatization policy followed so far has produced dismal results. A study of the Asian Development Bank reveals that of the total of 83 privatized units, only 22 performed better than under public sector management; the performance of 44 per cent remained at about the same level and 34 per cent did worse than before. Some buyers stripped assets and sold the real estate involved. No less than 20 industrial units that included fertilizer, cement, steel and ghee plants were closed, causing serious loss of output, employment and tax revenue. All this highlights the need for the government to undertake privatization through a carefully modulated strategy that keeps the national interest and the public good foremost in mind. In this endeavour, the experience gained so far should prove to be an asset.