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Is Industrial Privatisation A Viable Economic Policy For Development? An Analysis Of The Privatization Of Public Sector Manufacturing Industries In Pakistan

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IS INDUSTRIAL PRIVATISATION A VIABLE ECONOMIC POLICY FOR DEVELOPMENT? AN ANALYSIS OF THE PRIVATIZATION OF PUBLIC SECTOR MANUFACTURING INDUSTRIES IN PAKISTAN

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1. INTRODUCTION

The world today is witness to phenomenal and unprecedented strides in growth and development in an increasingly polarized fashion (Safier, 2005). Why global disparities occur and how they can be mitigated are fundamental questions that lie at the heart of the development debate. In an attempt to answer these questions, two schools of thought, namely the "neo-liberals" and the "structuralists", have surfaced in development literature with fundamentally different ideological stands and often divergent perceptions on the historical interpretation of facts. Such ideologies and related strategies have shaped and continue to shape the conceptualization and realization of development across the globe, especially in developing countries, often placing the relationship of the stakeholders of the process, namely the state, society and markets, under the spotlight.

In the current paradigm of neo-liberalism, which lays its faith in market-led growth for development and forms the foundation of economic globalization recipes professed by the likes of World Bank and IMF, the role of the state as an agent for development (Thomas & Allen, 2000) is not only questioned but also increasingly minimized. One vigorously employed policy prescription, for directly limiting the ability of the state to influence development administration and planning in much of the developed and developing world, has been the privatization of state-owned or public sector enterprises.

Privatization, which is not only an economically but also a politically motivated process (Clifford, 1993), has produced mixed social and economic results over the years following its introduction in the industrial, service and financial sectors of nation states. Although the roots of its implementation are often traced to the zealously pursued privatization programme of Margaret Thatcher's British Government during the 1980's, Megginson (2005) identifies the German government's efforts to sell majority stakes in Volkswagen and the chemical firm VEBA between 1961 and 1965 as the first instance of modern privatization programmes. Nevertheless, the true rise of privatization did occur after the policies of the Thatcher Government, the perceived success of which laid the foundations for the spread of privatization in most industrialized countries including Japan, France, Italy, Sweden and the USA. The developing countries also followed (or were compelled to follow) suit during the 1980's and 1990's, marking an embrace of privatization programmes by much of Latin America, Asia and Africa as well as the transition economies of central and eastern Europe (Megginson, op. cit.).

Today privatization programmes continue to run in varying manifestations across the globe driven by what Bienen & Waterbury (1989: 618) call "a spirit of pragmatic reaction to at least three decades of failed experiments in public enterprises". Whether this reaction is essentially pragmatic or not is again a question of ideological stance and interpretation of facts. Moreover, whether this "spirited reaction" is organic to the implementing country or externally imposed by multilateral and sovereign powers, puts the "pragmatic" nature of privatization programmes under greater suspicion. Nevertheless, the complete failure of this policy in some sectors of some countries, its resounding success in others and sobering effects in yet many others (Weizsäcker, Young & Finger, 2005) does not only invoke decades of raging debates on the generic pros and cons of privatization but also re-directs the spotlight on the political economy and the structural heterogeneity of different countries. Consequently, an in-depth look into a specific dimension of a particular country is essential for understanding the effects of privatization practice, especially in a developing country context.

1.1 Relevance of the Study and Proposition

Pakistan formally initiated her privatization programme in 1991, which has continued over the years in leaps and bounds. The programme however has consistently drawn criticism for its objectives, processes and results (Zaidi, 2005), while a new streak of disapproval has been provoked by the current policy of the government to pick up the pace of privatization and open doors to foreign ownership (Ziauddin, 2006; Ghausi 2006b; Khan, 2006).

Although privatization in Pakistan is being pursued in the financial, services and manufacturing sectors alike, the ensuing effects on these sectors require independent and in-depth analysis in their own right. Consequently, this paper critically analyzes the political and economic dimensions of the rationale, process and outcomes of the privatization of Pakistan's public sector manufacturing industries, and argues that privatization of these industries in its current manifestation is not a viable economic policy option because the economic and social disadvantages at both the micro and macro level ensuing from the implementation of this instrument outweigh its advantages. The paper however concludes that it is not the tool of privatization *per se* which is inherently flawed, but the context of Pakistan's political economy and the manufacturing sector as well as the privatization rationale, technique and process, which have shaped ensuing results and have rendered privatization in its current form as an unviable policy option.

1.2 Key Concepts

Privatization, like many other policy concepts has a "cluster of overlapping meanings" (Weizsäcker *et al*, 2005: 4). The term is broadly used to "describe a range of different policy initiatives designed to alter the balance between the public and private sectors" (Cook & Kirkpatrick, 1988: *3*) by restricting the role that governments play in using the resources of the society to produce goods and services and increasing that of the private enterprises in such matters (Weizsäcker *et al,* op. cit.). But before any analysis of what constitutes privatization is undertaken, it is important in the context of this paper to distinguish precisely what does not. A clear distinction therefore is necessary between the concepts of liberalization, deregulation and privatization, which are different yet interrelated policy concepts.

Liberalization, as understood by UNRISD (2005: 1) is the "reduction… in government intervention in markets… (and)… involves giving product and factor markets greater responsibility in the resource allocation in an economy", types of which may include financial, capital account, trade and labour market liberalization. Deregulation on the other hand constitutes "the removal or attenuation of restrictions, including requirements and prohibitions, imposed by a public authority on the actions of public or private actors" (Weizsäcker *et al,* 2005: *4*), while privatization entails the partial or full transfer of ownership or ownership rights of assets from public to private hands (Weizsäcker *et al,* op. cit.) or a kind of public-private partnership in which the public sector forgoes some form of control, management or operations to the private sector (Clifford, 1993). Although privatization and deregulation often go hand in hand, it is important to note that both these tools can and are used independently of one another and in their own right (Starr, 1988).

In the context of this study however, the term privatization refers solely to the transfer of complete or majority of ownership of assets along with management control from the public sector to the private sector, which is also known as divestiture (Cook *et al*, 1988; PES, 2005). Various modes of privatization associated with divestiture include public offering, secondary offering, third party sales (comprising auctions or negotiated sales) and mixed sales, which are concepts that shall be used within the analysis (Welch & Frémond, 1998) (Table-1.1).

Manufacturing industry, on the other hand, is defined as a "particular way of organizing production … (entailing) a constant process of technical and social change which continually increases society's capacity to produce a wide range of goods" (Hewitt, Johnson & Wield, 1992*:* 6). Production processes characteristic of industry thus include "complex techniques…(,) sophisticated machinery…(,) wide range of raw materials…(,) complex division of labour…(,) diverse range of skill

…(and)… use of technology" (ibid). Within this framework, Pakistan's manufacturing industry, which excludes services and extractive industries, involves production of finished goods from raw materials (Hewitt *et al,* op. cit.), and includes industries such as textile, metal works and fabrication, chemical, engineering, automobile, fertilizer etc and agro-based industries (PES, 2006).

The terms "industrial units" and "manufacturing units", also used interchangeably in Chapter 3 and 4, refer to the companies/complex/factories/firms/mills that are/were functioning under their respective holding companies collectively organized under the auspices of the MoIPSI. This generalization is necessary for analysis from two angles; one, the referred studies and the PC categorize "units" in this fashion (see Kemal, 2000; Naqvi & Kemal, 1991; PC, 2006d) and two, the variety and complexity of manufacturing 'units' in Pakistan's public sector demand such a generalization (for instance Pakistan Steel is both a corporation and a unit in itself). Moreover, unless otherwise specified, Chapters 3 and 4 use the terms "manufacturing industry" and "industry" interchangeably.

Table 1.1 – Common Divestiture Techniques

Type	Features
Public offering	Public share offerings on stock markets Used when enterprise is of sufficient size and quality, and markets are mature Often helps raise additional capital Can broaden share ownership Shares can be offered on the domestic and international markets
Secondary offerings	Public offering of shares already traded on domestic or foreign markets Setting of share price less difficult because shares have a market price Sold by brokers to individuals and institutional investors in a way similar to initial public offering
Third party sales	Enterprises not of sufficient size and quality are sold through third party sale of assets or shares Two methods used namely auctions and negotiated sales
Auctions	More common and transparent than negotiated sales Involve an open bidding process May involve a separate technical bid and financial bid
Negotiated sales	Used when there is 'only one bidder or a bidder has a marked advantage over other bidders in the government's eyes' (p.33) Involves negotiating an agreement that is both attractive to the buyer and protective of government interests Difficult to get the highest price in such sales Method is less transparent than auctions
Mixed sales	Combines two or three sale methods Allows several types of investors to participate in the transaction Used when an enterprise is 'sold to a strategic investor bringing capital, know-how, and market connections to the privatized firm' (*ibid*) Level of control offered may range from supermajority - 66 percent of voting rights absolute majority - 51 percent of voting rights relative majority - say, 35 percent of shares allowing principal majority

Source: Adapted from Welch and Frémond, 1998

1.3 Methodology

Published literature in the form of books and journals has been used for the literature review governing the conceptual framework, while the case-study of Pakistan draws on empirical studies, newspaper articles, published and unpublished literature as well as a personal interview.

1.4 Limitations and Constraints

Although a good amount of literature is available on the topic of industrial privatization, contemporary publications mostly address public services as opposed to public manufacturing. Consequently, in this paper, the attempt has been to integrate privatization and industrial policy literature.

A primary constraint in dealing with the case-study of Pakistan has been the scarcity of contemporary empirical studies establishing macro-level causality of the social and economic effects of privatizing public sector manufacturing industries. Although privatization has been accused to have played a part, econometric computations proving the same were difficult to find for some (not all) macro-economic elements, such as indicators proving post-privatization GDP and investment decline in the manufacturing industry. The analysis in Chapter 3 recognizes this caveat. Secondly, it was difficult to account for the effects of recent privatizations, because not enough time has lapsed for these effects to show.

1.5 Structure

The first chapter of this paper introduces the topic of privatization, substantiates the proposition of the study within the context of Pakistan's manufacturing industry case-study, defines key terms, identifies sources of information as well as related constraints and limitations, and lays down the structure of the study.

The second chapter begins with the theoretical debate on the role of the state in development, which establishes the foundation for subsequently detailing the micro and macro level debates on the advantages and disadvantages of privatization. This theoretical framework followed by an account of the writer's theoretical stance helps shape the conclusions of this paper in Chapter 4.

The third chapter is devoted to the case study of Pakistan. Taking a brief historical account of the political economy of privatization in the country, the first section of the chapter succinctly describes the rationale, objectives and process of privatization in Pakistan. The second section of the chapter, guided by the theoretical framework of chapter one, analyzes the micro and macro level advantages and disadvantages resulting from the privatization of public sector manufacturing industries in Pakistan.

Finally, the fourth chapter assembles the core debate of this paper in the light of the determined theoretical stance and the case study, validates the proposition substantiated earlier, and makes broad recommendations to guide future policy.

2. CONCEPTUAL FRAMEWORK

Development as we understand it today is a multifaceted concept encompassing an array of social, economic and political elements, which Simon (2003) terms as a "… process of predominantly positive change in the quality of life of individuals and society, in both material and nonmaterial aspects …" (cited in Agrest, 2004: 9). Nevertheless, precisely how development was understood during each paradigm of history essentially guided the formulation of strategies for its pursuit and defined the agents for its realization. Given this context, it is imperative to identify how over the years, development planning, which is "an effort to identify the most appropriate means and measures for achieving specific development objectives" (Martinussen, 1997: 228), has allowed markets or the state to take the lead in "acting on behalf of others to promote improvements" (Thomas *et al*, 2000: 189) and what was the theoretical rationale behind such undertakings.

2.1The State in Development Theory

The state as an institution for achieving the process of development and as an important initiator and catalyst of growth has held a cardinal position in much of the social science and conventional economics literature dealing with developing countries (Martinussen, 1997). Mindful of the differences within the dynamics of different states, Thomas *et al* (2000) identify certain

shared features of states, such as the monopoly of regulation and use of force within its boundaries, the promoters and providers of identity and cohesion, the agent and structure within a society requiring bureaucracy to "provide a framework for predictable social action" (p.191), a single entity and/or a complex combination of political institutions interacting with other agents of the society, and most importantly, a broader concept inclusive of the civil society and legal system but not equating to the often associated notion of government.

Characterized by the Platonics as benevolent, the neoclassical political economists and public choice theorists as an agency creating market distortions hindering effective development, the Marxists as an instrument serving the interests of the ruling class and the classical dependency theorists as subservient to international capital interests (Streeten, 1993), the capacities and actions of the state were theoretically interpreted within dogmatic extremes, until the state-centred theory of Myrdal surfaced in the development arena. His interpretation of the capacities of a "soft" state, which was unwilling to impose obligations of declared policy objectives on the governed (also unwilling to obey defined rules), helped describe the dynamics of the states in de-colonized developing countries, which neither had the capacity, nor the vision to broadly interpret economic development in a socio-political context. However, Myrdal insisted that the state *was* the most important institution for achieving progress and structural transformation and therefore needed comprehensive political and administrative reforms to effectively undertake its functions (Martinussen, 1997).

2.2 The Structuralist View on State led Development

Myrdal's case for the intervening role of the state belongs to the wider literature of debates professed by the structuralist school of thought.

2.2.1 Theoretical Underpinnings

The structuralists, who see development "as a process of transformation of economic and social structures" (Jenkins, 1992: 137) view developing countries as cases of certain special and rigid structural features that place them at a disadvantage in the free market system proposed by the classical economists. They essentially divide the world in a *centre-periphery* model according to which the developing periphery is structurally dependent on the developed centre that thrives on the logic of unequal exchange which characterizes international trade (Larrain, 1994). Polarization caused by free market mechanisms in both domestic and international arenas thus leads to highly unequal forms of ownership and control of resources which in turn negatively affect economic performance.

2.2.2 Strategies for Development

Building on Keynes's idea of the "appropriateness of relatively comprehensive state intervention … to promote economic development" (Martinussen, 1997: 356), the structuralists propose development through instituting the policies of industrialization, ownership control, technological advancements and capital accumulation, which require the state to directly intervene. They recommend that developing countries should pursue, amongst others, the strategy of ISI to achieve self-reliance through the local production of formerly imported goods (Jenkins, 1992). In such a pursuit, given the weak entrepreneurial class of developing countries and its inability to spearhead industrialization, the state must invest in lumpy and risky capital-intensive industrial projects. Other reasons for direct production include control of strategic sectors of the economy, such as steel or defence related industries (Chandra, 1992), retention of employment in failing private business entities through nationalization (Megginson, 2005), creation of a balance between economic sectors, distribution of income opportunities and growth in order to reduce spatial inequalities (Martinussen, 1997), overcoming issues of racial and/or ethnic disparities, stimulation of labour-intensive industries in order to generate employment, avoidance of private sector monopolies, equitable provision of social services and price control of intermediate goods that serve as inputs for other important industries (Chandra, 1992).

Secondly, in order to nurture industrial development, the institution of state-driven protectionist policies to limit

international competition is proposed. Thirdly, it is suggested that the structure of the industry must be defined by the state through specific policies in order to promote investment in priority areas and maintain a balance between large and small scale industries. Furthermore both international and local capital needs to be guided by the state for planned development. Lastly, it is argued that technological advancement and capital accumulation needs to be strengthened by the state through direct support or incentives and through borrowing and lending at low rates (Jenkins, 1992; Martinussen, 1997).

2.2.3 Central Argument

In a nutshell, the structuralists fundamentally argue that markets do not always function properly in developing countries, which leads to market failures, and that the actions of private individuals aiming at economic efficiency do not necessarily promote social efficiency (Rojas, 2005a). Given the negative distributional effects accompanying capitalist industrialization (Rueschemeyer & Evans, 1985) and yet the immense importance of industrialization in development, state intervention is considered absolutely essential.

2.3 The Neo-liberal View on State-led Development

The neo-liberal school of thought, in stark divergence to the structuralists, rejects the grounds for state intervention in development.

2.3.1 Theoretical Underpinnings

With an emphasis on a trickle-down approach to growth, neo-liberalists oppose the view that developing country conditions warrant the need of special economic theory and lay their faith in the markets to provide for economic growth. Drawing on the neo-classical assumptions of the utility and profit maximization of consumers and producers respectively as well as the central role of the market as the "determinant of economic behaviour" (Martinussen, 1997: 52), the unit of analysis of neo-liberals is individuals rather than structures, and the emphasis is on the flexibility of markets rather than the rigidity of structures. Neo-liberals argue that only a competitive market system will lead to an efficient economy through the optimal allocation of resources which are guided by non-distorted market prices. Consequently subsidies, exchange rate controls, low interest rates and wage rate controls will lead to under optimization of productive resources, low profits and higher costs ultimately causing inefficiencies, slow growth and high inflation, which will promote unproductive activities. Needless to say, neo-liberals believe that protectionism essentially promotes inefficiencies and rent-seeking behaviour. Furthermore for them, the comparative advantage theory of Ricardo still holds and a bias towards industrialization essentially means a depressing effect on agricultural production and investment.

2.3.2 Strategies for Development

Given these theoretical underpinnings, the neo-liberalists propose the roll-back of the state and introduction of free market mechanisms for development through the policies of market liberalization which includes the removal of price controls; financial liberalization and labour market liberalization; trade liberalization which calls for removing import quotas, reducing tariffs and instituting realistic exchange rates; and reduction in the direct role of the state which entails privatization and cuts in state expenditures. They further substantiate EoI as a strategy for integrating with the world economy (Jenkins, 1992) by opening up markets to foreign competition and exporting goods and services in areas of comparative advantage.

2.3.3 Central Argument

In a nutshell, neo-liberals criticize that in comparison to the allocative efficiency of markets, the state as an institution neither has the required capabilities, nor the necessary instruments to plan effectively (Jenkins, op. cit.). In addition, increased state spending does not only crowd-out private investment but also leads to budget deficits that ultimately cause high inflation. Furthermore SOEs, which are generally inefficient, low capacity utilizing, over-employed, indebted, loss making entities, also significantly contribute to increasing budget deficits and fiscal haemorrhage. Consequently, distortionary state intervention in development is considered unwarranted.

2.4 The Rise and Fall of State-led Development

Given the above mentioned theoretical stands, it is important now to take a look at how the world actually witnessed the rise and fall of state-led development since WWII.

2.4.1 Post WWII Scenario

As Jenkins (1992) explains, it was the Great Depression of the 1930's followed by the embrace of Keynesian philosophy of government intervention in the economic sphere by the likes of Britain and the US that undermined the belief of many theorists and countries in the free market system. This set the premise for building an ideological stance for state managed development which was characterized by the "use of state bureaucracy as an engine of growth and development, and as a central planning and allocation mechanism" (Martinussen, 1997: 258). These were the heydays of SOE growth in the industrial and infrastructure sectors of much of the newly decolonized countries (Martin, 1993).

2.4.2 Debt Crises and SAPs

However, it was the changing intellectual and political environment in the West and the debt crises of the late 1970's that turned the tables on this form of development (Jenkins, 1992). SAPs, which were initiated in the 1980's under the auspices of the World Bank and IMF as a lending conditionality to debt-burdened developing countries, were essentially designed on neo-liberal underpinnings to reduce the risk of further debt crises, by instituting macroeconomic reforms and the roll back of the state. These complemented by the Washington Consensus of 1990, which was a set of largely neo-liberal policies advised by "Washington-based institutions to Latin American countries as of 1989" (GTN, 2003: 1), unleashed a comprehensive programme to minimize the role and size of the state through policies of market liberalization, trade liberalization, privatization of SOEs and cut backs on expenditures.

In the later period of the 1990's however, following the disastrous social and economic consequences of the SAPs (Rojas, 2006d), the World Bank and IMF were compelled to recognize the importance of the state in development. This was clear from the World Bank's World Development Report 1997 that substantiated the role of the state as an institution ensuring the establishment of the foundations of law, maintenance of a non-distortionary policy environment including macroeconomic stability, investment in basic social services and infrastructure, and protection of the vulnerable and the environment (World Bank, 1997). Although these responsibilities entrust the state with the welfare of the society and the economic development of the country as a whole, the emphasis of most advocated policy recipes remained on a merely facilitative role, which ensured the smooth functioning of the market mechanism. As Martin (1993) opines, it is not a question today of whether the state should intervene or not but essentially of "how and to whose benefit" (p.48).

2.4.3 Current Paradigm

Consequently, in the current era of globalization where dominant neo-liberal policies continue to dictate the development trajectory of most developing countries, privatization remains very much on the agenda of the New Public Management toolkit (Rojas, 2006c) alongside other policy prescriptions propagated by the IFIs.

2.5 The Debate on Privatization

The development debate on the question of privatization has given rise to burgeoning literature on the viability of this policy instrument. Ideological stands backed by empirical country and firm level studies provide convincing "for" and "against" arguments, which have guided privatization programmes in many developing and developed countries over the years. Consequently, it is important at this juncture to identify what advantages or disadvantages privatization brings for a SOE, how if at all it influences firm-level efficiency and what if any broader social and economic benefits or problems result for the country as a whole. To capture a set of arguments encapsulating these fundamental questions specifically for industries (not including services), the following conceptual framework is divided into two major sections dealing with micro and macro level debates, the skeleton of which is inspired by the work of Sheshinski & López-Calva (2003) and

Perevalov, Gimadii & Dobrodei (2000). This framework will later assist in understanding the case of Pakistan, where it shall be ascertained whether the micro and macro advantages of privatization of manufacturing units have been greater than the disadvantages ensuing from it.

2.5.1 Micro-Level Arguments

Kaldor (1980), Megginson (2005) and Perevalov *et al* (2000) argue that the strongest case for privatization builds around the ideological stance that private ownership is more efficient than public. Efficiency here, as understood by Jones & Mason (1982) constitutes both allocative efficiency, i.e. the correct price-quantity bundle choice, and productive efficiency, i.e. minimum cost of production for the chosen quantity. The public choice theory and the property rights theory supplemented by the principal-agent argument provide the fundamental framework for this discussion, which mainly entails the concepts of incentives, ownership, monitoring & accountability and political interference.

2.5.1.1 Incentives and Efficiency

The grounds for private efficiency incentives shape up on the premise of the principal-agent theory, which is characterized by "a situation in which a principal (or group of principals (e.g. stakeholders)) seek to establish incentives for an agent (or group of agents (e.g. management)), who takes decisions that affect the principal, to act in ways that contribute maximally to the principal's own objectives" (Vickers & Yarrow, 1988: 239). However, given that the objectives of the principal (i.e. to maximize profit) and agent might diverge and that there may be information asymmetries between the parties, the principal must enter the agent into a monitoring-reward system via contract (Martin & Parker, 1997).

For Arguments: Given such a principal-agent relationship, strong incentives for efficiency and innovation arise for private firms (Weizsäcker *et al,* 2005), which according to the property rights literature occur due to the clear definition of the rights to profit (Martin *et al*, 1997). For the SOEs, however, incentives for efficiency are weak because the state is representative of distinct groups of politicians and civil servants (Aharoni, 1982) that forces the firm to satisfy multiple, vague and uncertain political objectives of a bureaucratic line of command (Martin *et al*, 1997).

Moreover, Megginson (2005) argues that increased revenues cannot personally benefit the SOE management and reducing costs essentially implies antagonizing workers and suppliers thereby increasing personal costs, which serve as adverse incentives. In a world far from information symmetry, SOE inefficiency can also be understood through the interpretation of the incomplete contract theory by Schmidt (Megginson, op. cit.), who asserts that given the willingness of the state to provide subsidies for enterprises (soft-budget constraints) in a situation where political overseers cannot perfectly observe the costs, incentives to SOE managers for controlling costs, who alone are aware of the true estimates, become even less.

Furthermore, it is argued that efficiency incentives for SOEs are minimal because they are not under the threat of bankruptcy or takeover due to state patronage, which in a free capitalist market is a major incentive (Vickers *et al*, 1988). Lastly, in a monopolistic situation, Megginson (2005) stresses that incentives for both allocative and productive efficiency are minimal because customers are unable to choose between options, leading to very little market pressure for improvement and wastage of resources, which private ownership and competition do not allow for. Supporting evidence for these claims is given by La Porta and Lopéz-de-Silanes, who in a 1997 study of 218 non-financial highly unprofitable Mexican enterprises privatized during 1983-91, show that profitability after privatization increased (cited in Kikeri & Nellis, 2004)

Against Arguments: Contesting this stance, Martin *et al* (1997) argue that the property rights theories are essentially based on the naïve assumption of the rational and maximizing individual. This they stress may be true in sole proprietorships and small companies, but cannot be attributed to privatization *per se,* as such forms of business are not alternatives for state ownership, which are often replaced by joint stock companies. In such companies, where ownership and control are separated, incomplete contracts (i.e. imperfect

monitoring-reward systems) and information asymmetries between the board of directors and shareholders, lead to managerial non-profit discretionary behaviour primarily because the management itself rarely has a stake in the company (except for the directors). Moreover, quoting Jenkinson and Mayer on hostile takeovers and managerial efficiency, they argue that managers under consistent threat of a takeover and self-removal "discount the long-term future performance of the company" because there is little sense in initiating projects whose benefit will be reaped by others (cited in Martin, op. cit. p.23).

In the same vein, Sheshinski *et al* (2003) who elaborate on Williamson's work of 1985, point out that given "the impossibility of writing complete contracts with the private owners (,) … SOE(s should) … function at least as well as privately owned firms (under the same conditions)" (p.430). More importantly, Martin (1993) argues that because the public sector does not always prioritize profits and has social goals in perspective, its character *is* different from that of the private and it should therefore be assessed with different criteria of performance judgement. Empirical evidence presented by Bozec, Breton & Côté (2002) using a sample of SOEs and private firms of various countries between 1976 and 1996, also shows that when the main goal of SOEs is profit maximization, they perform at least as well as their private counterparts. In conditions of significant market failure such as tendency for natural monopolies, large-scale initial investment requirements and positive externalities (Dávila, 2006), Sappington and Stiglitz (1987) argue that public ownership reduces the transaction costs of state intervention in the economy (cited in Megginson, 2005), while Cook *et al* (1988) insist that privatization especially in developing countries which experience pervasive market failures, have weak state institutions and capital markets, and rely on primary and non-diversified exports, will be nothing short of a disaster.

2.5.1.2 Ownership and Efficiency

For Arguments: Meggision (2005), citing the work of Hayek in 1994, opines that in a competitive market where prices guide allocative efficiency, operational efficiency of a private firm is even greater. However, any "misinterpretations" that competition supersedes ownership is rejected (OECD, 1996), which according to Kikeri *et al* (2004), who studied the empirical work of Sachs, Zinnes and Eilat in 24 transition economies, is imperative for but not a guarantee of performance improvements, therefore necessitating change of ownership.

Against Arguments: On the contrary, Perevalov *et al* (2000) based on their study of 189 industrial enterprises in Russia between 1992 and 1996, conclude that change of ownership by itself "on average does not produce performance improvements, except for costs per unit of revenue and to some extent for productivity of labour" (p.351). Cook *et al* (1988) in their research on the contributions of 15 economists from different countries also interestingly conclude that an "improvement in the economic performance of the public enterprise sector is more likely to result from an increase in market competition than from a change in ownership" (p.31). On the other hand Kay and Bishop, moving away from markets and stepping into the domain of management, deduce from their 1988 research on the before and after privatization TFP of several British companies, that "change in culture and management methods rather than in ownership … (is) the decisive influence on changes in results …" (cited in Martin, 1993: 140).

2.5.1.3 Monitoring & Accountability and Efficiency

For Arguments: The property rights theory, which recognizes agency problems in all forms of ownership, stresses that because private ownership is transferable through capital markets, optimum allocation of resources occurs and stakeholders assert a monitoring pressure. Furthermore, stakeholders can also hold the company accountable through Annual General Meetings besides simply trading shares (Martin *et al,* 1997). Megginson (2005) argues that because of dispersed citizenry and asymmetric information between managers and political overseers to the advantage of the former, collective action problems of high costs of monitoring and low returns to SOEs leads to inefficient functioning.

Against Arguments: On the other hand, Vickers *et* al (1988) deny that there will be unanimity in the way shareholders rank different policies of the firm's management especially if the shareholders are also consumers of the firms produce. In such a scenario, their decisions do not remain limited to managerial activities influencing financial returns only, thereby affecting effective monitoring. Contesting the discipline of capital markets exerted upon the private management, Martin *et al* (1997) stress that this is far from perfect, because inertia and trading costs of shares may not allow the movement of funds towards areas of higher returns. They also point to the possibility that in dispersed shareholder ownership where no individual or group has the incentives and power to "exercise control and ensure profit maximization" (p.21), agent monitoring may be improved through instituting single ownership such as that in a public entity.

2.5.1.4 Political Interference and Efficiency

For Arguments: According to public choice theorists, the behaviour of politicians and bureaucrats concerning SOEs is personal instead of public utility maximizing, which leads to possibilities for rent-seeking and hiring of politically connected managers rather than those with the best abilities, which consequently promotes inefficiency (Vickers *et al*, 1988; Hemming & Mansoor, 1988; Perevalov *et al*, 2000). Boycko, Shleifer & Vishny (1996) also argue that because SOEs pursue the non-economic objectives of politicians, such as excess employment to ensure future votes and building industries in politically sound areas, SOE functioning becomes undesirably inefficient while objectives of interest groups are satisfied. Privatization, as concluded by them, effectively de-politicizes an enterprise by curtailing political discretion.

Against Arguments: However, Martin *et* al (1997) insist that the public sector is not homogenous and not all bureaucrats should be expected to act in a corrupt manner. The possibility that politicians and civil servants could sometimes act in public interest, should be kept in mind. On the other hand, Cook (1997) argues that "privatization, as with public enterprises, (also) offers politicians a means of buying votes and rewarding friends" (p.894), which keeps corruption very much in the picture. Perevalov *et al* (2000) also cite that in a weak institutional climate, private firms do not have the incentive or ability to keep their assets in good shape over the long run, resulting in speculative short-term behaviour, which is undesirable as opposed to long-term political interference that may be desirable for performance improvements. Lastly, Martin (1993) stresses that not all public sector employees are incapable performers and most have credentials and capacities compatible with labour market standards. The need, he urges is to provide them with managerial tools rather than substitute them for private management.

2.5.2 Macro-Level Arguments

In the macro-level framework, the case for privatization derives impetus from the idea that because loss-making SOEs are financed by state loans (or state guaranteed loans) and socially desirable objectives of SOEs are achieved through state subsidies, heavy fiscal burden is experienced by developing country governments which leads to many economic ills such as inflation. In fact the World Bank has correlated higher shares of SOEs accounting for GDI with lower rates of economic growth (Jenkins, 1992). Privatization would therefore be a relief to taxpayers and a source for bridging the fiscal deficit of developing country governments by ridding them of loss-making SOEs and redirecting funds from asset sale to the cause of debt and fiscal relief. Efficient private enterprises substituting these loss-makers would pay more taxes in a progressive tax system, thereby increasing revenues, which would ultimately benefit the poorest (Birdsall & Nellis, 2003). It is denied that privatization causes job loss, and is asserted that improvements in productivity lead to new job creation and better terms of service (Kikeri, 1998). On the other hand, privatization programmes poised to attract FDI through mergers and acquisitions are also credited with bringing in much needed benefits of technology transfer, job creation, export expansion, and reduced balance of payment adversities (Singh, 2005). Finally, privatization through public offering in capital

markets is said to widen share ownership and enhance distribution of assets and wealth within the society (OECD 1996; Starr 1988).

Macro-level benefits however form the weakest case for privatization, opposition to which draws vehement criticism (Cook *et al*, 1988; Cook & Minogue, 1990; Starr, 1988; Singh, 2005) especially in the areas of economic growth and performance, wealth and asset distribution, foreign ownership and industrialization, unemployment, feminization of workforce and income inequality, and strategic national interests.

2.5.2.1 Economic Growth and Performance

Sheshinski *et al* (2003) caution that macroeconomic evidence required to establish a causal relationship between privatization and macro-economic indicators is difficult to substantiate because the influence of other events on the overall results is hard to isolate. With this caveat in mind, Starr (1988) absolutely rejects the notion of the likes of World Bank that public sector growth impedes economic growth, calling such an idea as unwarranted extrapolation of inefficiency in public enterprises. Hoeven & Hoppe (2005) however, using the 2004 Report of the World Commission on the Social Dimension of Globalization, empirically show that contrary to the popular belief, the last four decades of liberalization and privatization have brought decreasing and not increasing global growth rates. Cook *et al* (1988) using country level studies substantiate that "the size of the public sector *per se* does not have a significant bearing on the performance of the sector or economy" (p.10).

On the other hand, Birdsall *et al* (2003) also claim that the benefits of privatization on state budget are not very well established. They cite an IMF review of 18 privatizing countries, which informs that gross receipts from privatization accounted for about 2% of GDP, but comment that nearly half of this amount is often eaten up by "high costs of financial cleanup, labor downsizing and sales assistance" (*p*.1621) which leaves little margin for debt and fiscal relief. In a similar tone, Cook *et al* (1988) explain that asset sale revenues do bring about reduction in fiscal deficit. However the usual practice of providing incentives for privatization could mean a probable low pricing of a productive asset, which may not be reflective of the discounted present value of future flows of revenue had this enterprise been retained.

2.5.2.2 Distribution of Assets and Wealth

Birdsall *et al* (2003) through their study of privatization in Latin American and transition economies contest the distributional logic of privatization and state that in the trade-off between equity and efficiency, nearly all privatization programs have favoured the latter. They conclude that "many privatization programs have worsened the distribution of assets …, at least in the short-run" (p.1617), with transition economies experiencing larger increases in inequalities than Latin America. Starr (1988) also points to the privatization consequence of wealth concentration in the hands of a few, which serves as a means of altering the social class order. Citing the example of privatization in Chile during the 1970s, he brings attention to the "vast shift in wealth (which) took place with the privatization not only of industry but of the financial assets of the social security system, which ended up concentrated in the hands of a few private financial groups" (p.18).

Another aspect of distribution of wealth becomes obvious when privatization leads to transfer of wealth in the hands of economically and politically dominant ethnic and racial minorities (Bienin *et al*, 1989), thereby creating further disparities between them and the majority group.

2.5.2.3 Foreign Ownership and Industrialization

Privatization focused on attracting foreign owners who bring with them much desired FDI, has the same crowding out effect on domestic capitalists as (allegedly) state intervention in direct production. In this regard, Ferraz, Kupfer and Iootty (2004) argue through their study of the ownership nature of Brazilian industry, that the country may soon face a development dilemma because "history suggests that local capital and innovation capabilities have been outstanding features of countries successful in achieving sustained economic development" (p.91).

From another angle, the more specialized a nation becomes through its foreign affiliates to cater to TNCs, the more resources will flow towards building "supplier industries", which will mean a shrinking, dependent industrial base of the economy (Rojas, 2005b). The increased propensity of exports in the host economy due to specialization will force the country to import items of domestic needs at higher prices than at what it could produce itself, leading to a distortion in the balance of payment.

On the other hand, Singh (2005) also warns developing countries of the dangers in considering FDI as a panacea for development, especially due to the unstable nature that it has acquired over the years. This volatility is particularly visible in times of imminent financial crisis, when TNCs indulge in hedging activities to cover exchange rate risks thereby generating added pressures on the host country's currency and posing further macroeconomic problems. On mergers and acquisitions, Singh (2005) notes that "61% of mergers between 1995 and 2001 (actually) destroyed shareholder wealth" (p.87) instead of increasing it. Other problems of capital flight, transfer pricing, non-transfer of core-technology and speculative behaviour (UNCTAD, 2002; Rojas, 2005b) question the viability of privatizing national assets to global capitalists, whose footloose movement in and out of areas of comparative advantage offer severe macroeconomic constraints.

2.5.2.4 Unemployment, Feminization of Workforce and Income Inequality

Starr (1988) is of the view that privatization may have little if any progressive effect on income distribution. Motives for productive efficiency call for employing labour at low wage rates thereby exacerbating income inequalities. Furthermore, direct job loss is caused in layoffs following privatization and reform. This is empirically substantiated by Bhaskar & Khan (1995) who conclude in their study of the jute industry of Bangladesh that "privatization has reduced employment significantly" (p.267). Furthermore, deducing from the study of 2200 manufacturers in China, Armenia, Georgia, the Kyrgyz Republic, Russia and the Ukraine, Hoeven *et al* (2005) cite that there was a 10% average overall loss of jobs due to privatization.

Standing (1999) describes how the rejuvenated faith in markets, roll-back of the state and commoditization has increased income insecurity due to falling wages, job insecurity due to part-time contractual employment as against permanent public sector jobs, and loss of entitlements, causing what he calls the feminization of labour. Hoeven *et al* (2005) also point to a gender dimension of privatization, whereby women suffer the most given that their "largest absolute employer" (p.269) happens to be the public sector. The fate of labour unions is also bleak, which in the wake of privatization are not only being eroded but also marginalized. This was the case in the privatization of the Polish industry, which led to the weakening of labour interest representative institutions (Towalski, 2002) leaving workers exposed to the potential exploitation of private owners.

2.5.2.5 Strategic National Interests

Starr (1988) is of the view that "the privatization of enterprises with strategic military or economic significance raises especially sensitive questions of sovereignty and security" throughout the world (p.15). According to him, the conflict between privatization and strategic considerations is greater for weaker states in the global economy, while strong countries, "knowing that they can privatize without jeopardizing their sovereignty, lecture the weak on the perils of state enterprise and restrictions on investment" (ibid). However, more recently, the US Congress forced the UAE based Dubai Ports World to handover P&O – a British company running six major US ports from New Jersey to New Orleans which it took over in 2006 – to a US firm (BBC, 2006) because an undertaking of such strategic nature by an Arab state was viewed as a compromise of national security.

2.6 Bridging the Public/Private Divide – A Flexible Approach Towards Privatization

The above-mentioned debate on state vs. markets and public vs. private – although not exhaustive – points to an important theoretical underpinning relating to the dichotomy of state *or* markets and public *or* private, the validity of which is doubtful in the

presence of hybrid institutions (Streeten, 1993) such as joint-stock companies, cooperatives and public private partnerships, as well as concepts of governance instituting the optimum roles of not only markets and states, but also the all important civil society in development. Consequently, it is not the "absolute size of the public sector and the quantity of state intervention … (that is important but) … what is economically and politically feasible at a given time" (Martinussen, 1997: 266) and "what may be the most appropriate division of labour between the … (state and markets which may) avoid(…) or compensate(…) both state and market failures" (p.265).

It is also clear from the literature that the proposed significance of privatization as a policy option for developing countries, which are by no means homogenous, "has been greatly exaggerated" (Cook *et al*, 1988 p.127). This is true not only because privatization "evokes sharp political reactions" (Starr, 1988: 1) in fractured developing country societies, but also because "LDCs contain within them as much variance in economic characteristics as that existing between them and the advanced industrial countries" (Bienen *et al*, 1989: 630). The political economy of privatization in developing countries thus warrants a thorough contextual insight within a broad intellectual, historical and global framework maintaining an eye on the institutional setting and power distribution in a given society (Young, 2005a).

Whether pressures for privatization are organic or externally imposed is yet another angle which determines its success or failure in developing countries. The extent of political action required to bring about economic and political restructuring ordered by privatization is determined, in part, by the source of "reformist pressure" (Cook *et al,* 1990: 399), which in the case of many developing countries, happens to ensue from loan conditionalities characterizing the wider package of SAPs (Clifford, 1993).

Such an understanding however does not go to say that privatization never works, or never produces the desired macro and microeconomic effects that it is expected to bring about. No doubt several public sector industries in many developing countries are not only inefficient but are, as proven by IMF studies, sometimes not fulfilling their distributional goals either (Cook *et al*, 1988). However, causal inference that "existing public enterprises are not capable of achieving significant improvements in efficiency" unless privatized points to dogmatic perceptions of privatization as a panacea and as the only policy resort (Cook *et al,* op. cit. p.31). Evidence from Bangladesh during the 1980's and 1990's, when 50% of privatized small manufacturing units had to close down, while that from Sri Lanka, where six bankrupt companies had to be renationalized (Betz, 2005) refutes the ownership=efficiency claim of privatization. Moreover, successful public industries in developing countries such as Korea, Brazil and China have also demonstrated that they can be profitable and efficient entities competitive in both local and export markets (Box-2.1).

In a nutshell, the success or failure of a firm is fundamentally "a function of to what extent, and in what direction, its owners exercise the authority that comes with ownership and its managers carry out their jobs" i.e. the right culture, clarity of goals and institution of systems that foster the fulfillment of these goals (Wortzel & Wortzel, 1989: 633). Consequently, viable policy alternatives and/or approaches to privatization, which may complement or substitute this tool, encompass the establishment of a competitive environment coupled with an effective regulation system warranting a strong state with able capacities. Furthermore, improved management styles and techniques, which form the heart of efficient and effective functioning, through reforms constituting better hiring and incentive mechanisms, can greatly improve performance as well (World Bank, 1983). Possibilities of public-private partnerships can also be explored for industrial management in order to seek the best mix of the two development agents. The third development agent, namely civil society also has potential, where universities, foundations and other non-profit institutions (Weizsäcker, Young, Finger & Beisheim, 2005)can assist in areas such as skill enhancement and technological improvements. Through such a mix of control and leverage, performance constraints on industrialization could be

eased while the state would still be in a position to subtly guide the course of industrialization within the country.

Box 2.1 Impressive Performance of State-Owned Enterprises in China

Decades of enterprise restructuring in China's public sector has paid off for the economy. Attempts to turnover loss making industries into viable businesses through instituting a corporate culture in almost all state-owned enterprises and transforming them into joint stock companies, has allowed for massive strides in performance and quality improvement in the Chinese public sector.

During 2001, state-owned enterprises accounted for 50% of profit gains from China's industries, creating an aggregate industrial output value of 2,178.33 billion Yuan[1] to register a 13% increase in real terms over that of the previous year. Moreover, 3,865.73 billion Yuan of operating income and 192.12 billion Yuan worth of export delivery was also recorded during the same period, which was respectively a 7.6% and 7.8% increase from the previous year. According to the State Key Enterprises Development Report 2001, 83.6% of China's key state enterprises (428 industrial units) operated with a surplus, amounting to total profits of 244.39 billion Yuan, which was a 7.2% increase from the previous year. Only 16.4% of the total i.e. 84 units were registered as loss making enterprises during this period. With key state enterprises claiming an annual per-capita industrial yield 19,000 Yuan higher than the national average, an asset debt rate 5% less than the national average and interest gains 1.3% higher than the national average; the performance of state-owned industries has been nothing short of impressive. Another feather in the cap for public sector enterprises came when, with increasing profitability, performance gains and a step-up on R&D for new product development, six Chinese enterprises made it to the list of the world's top 500 enterprises in 2001.

In 2004, 42.4% of the total industrial value added created by the entire Chinese industry was produced by state-owned enterprises. 370 enterprises in China's top national 500 list were state-owned and state stock-holding enterprises, boasting assets of 27,370 billion Yuan and profits worth 266.3 billion Yuan. The year 2004 also saw 14 state-owned enterprises amongst the prestigious list of the world's top 500 enterprises. As of date, China's state-owned enterprises still employ half of the country's 750 million workers and control 57% of its industrial assets.

Sources: PDO ,2002; GOV.cn, 2005; Kikeri & Kolo, 2006

[1] 1 US$ = 7.99 Yuan; Forex rate as on Aug 16th, 2006 (Economist, 2006)

3. CASE STUDY OF PRIVATISATION IN PAKISTAN'S PUBLIC SECTOR MANUFACTURING INDUSTRIES

Strategically located in the region of South Asia (see Annex-A) (Hilali, 2005), Pakistan formally initiated her privatization programme in 1991, although occurrences of denationalization date as far back as 1977 (Zaidi, 2005). Under what circumstances and in what way did the drive for this initiative develop and foster over the years, essentially formulates the basis for understanding the micro and macro level consequences of privatization in Pakistan's public sector manufacturing industries, which are the two central themes discussed in this chapter hereon.

3.1 The Political Economy of Industrial Privatization in Pakistan: A Historical Account

A society's political economy, which includes "basic (economic) structures and power relations …(, essentially draws the wider) limits within which the form and impact of economic policies" is determined (Martinussen, 1997: 242). The specifics of these determinants amongst many others include the type of regime, capacity and efficiency of state bureaucracy and institutions, and the nature of chosen development strategy (Martinussen, op. cit.). Consequently, the form and impact of Pakistan's public sector manufacturing industry privatization programme can be largely gauged through the political and economic conditions of the country, which have been captured in the following historical account of events.

3.1.1 Strengthening of the Private Sector through State Intervention

During the 1950s and 1960s, which is considered as the peak time of Pakistan's economic growth (Zaidi, 2005), the state made a conscious effort to directly intervene and strengthen private sector capacities through a network of institutions, as part of the larger ISI strategy adopted soon after independence in 1947. Amongst such institutions was the PIDC which was setup in 1952 with the mission to establish and run industries in areas neglected by the private sector "either due to technological complexity or the lack of immediate profit return" (Zaidi, 2005: 143) and subsequently transfer profitable undertakings to private hands. In this regard, PIDC established amongst others, several heavy engineering, chemical, jute and fertilizer industrial units, some of which were later sold with a view of strengthening private sector capacities and maintaining regional industrial balance within the country. The efforts of PIDC were also complemented by the DFIs of PICIC and PIFCO, which were entrusted with providing much needed credit support to the private sector.

3.1.2 Period of Nationalization

Although the contribution of the above-mentioned institutions was commendable in spurring industrialization, wealth concentration during 1958-1970 soared to enormous heights whereby only "twenty-two families controlled 66 per cent of (the country's) industrial assets, 70 per cent of insurance and 80 per cent of total banking assets" (Zaidi, op. cit, p.102). The subsequent period of 1972-1977, which followed the separation of East Pakistan (Bangladesh) and was characterized by the then government's "experiment with socialism" (Hasan, 1998 cited in Srinivasan, 2003: 3), witnessed considerable expansion in the public sector following a massive nationalization programme of basic industries and financial institutions (Bokhari, 1998). The vegetable oil industry, 31 large firms in 10 basic industries and 2,000 rice, flour and cotton ginning mills were amongst the manufacturing units nationalized during that time (Zaidi, 2005) (Box-3.1).

3.1.3 Groundwork for Future Privatization

While the pre-privatization performance of public sector manufacturing industries will be discussed in detail at a later point, it is enough to say at this juncture that domestic "economic turmoil, … external shocks, economic dislocation and disruption" (Naqvi & Sarmad, 1993 cited in Zaidi, op. cit: 108) caused by capital flight, low investor confidence, the oil crisis and unsuitable industrial policy led to an overall underperformance of the economy which also affected public sector industries. Consequently, the first denationalization of industrial enterprises occurred in 1977 when the then MLA announced the

denationalization of 2,000 rice, flour and cotton ginning mills (Bokhari, 1998; Zaidi, 2005). In 1980, Pakistan also signed her first long-term EFF agreement with the IMF, (Zaidi, op. cit.). In order to infuse greater efficiency in public sector industries, the EAC in 1981, under the auspices of the then Ministry of Production, embarked upon improving the performance of 56 manufacturing units through the institution of a performance signalling system[1] (Bokhari, 1998; Zaidi 2005). Nevertheless, by 1985, the Cabinet Committee on Disinvestment was formed, which identified loss making industrial units for potential privatization but made no practical headway (Bokhari, 1998).

3.1.4 Beginning of Pakistan's Industrial Privatization Programme

It was the year of 1988 when SAPs actually began to dictate "Pakistan's economic policies, management, and performance …(to the effect that) (a)lmost without exception, the policy measures undertaken by the various governments in power since (1988) follow(ed) very closely the details in the Policy Framework Papers" (Zaidi, 2005: 336). Consequently, the civilian government of 1990, "bound by the covenants of the (structural adjustment) agreement" (ibid), marked the formal beginning of a widespread privatization programme in Pakistan. Privatization was declared the "primary economic policy objective" of the government, and a plan to divest 118 SOEs was subsequently approved (Bokhari, 1998: 3). In order to realize this plan and to institutionalize privatization in the country, the PC was established alongside the CCoP, which is the approving authority of PC's recommendations. The Economic Reforms Order of 1972, which was the legal tool for nationalization, was also countered by the ratification of the Protection of the Economic Reforms Ordinance 1991 (Bokhari, op. cit.).

Box 3.1 Organization of Public Sector Manufacturing Industries in Pakistan

Structure: All companies in Pakistan's public sector are incorporated either under the Companies Act 1913, the Companies Ordinance 1984 or 'under special legislation of the federal and provincial governments' (p.1). Such companies can either function independently or work under the management of respective corporations. In the case of the manufacturing sector, industries are "grouped and managed by sectoral holding corporations" (p.2) which are in turn supervised by the MoIPSI. Initially, SOEs were established solely through GoP equity capital while the acquired shares of nationalized industries "were transferred to the respective corporations in exchange for corporation stocks" (ibid). Moreover, the development loans extended to various holding corporations "were converted into preferential and ordinary stock'" (ibid). Consequently, holding corporations not only manage public industries but also hold all or majority of equity in them on behalf of the GoP.
Recruitment: It is the Prime Minister of Pakistan who appoints the chairman and management board members of corporations. Staff below the level of general manager is appointed by these boards of management, while appointment of general managers requires the approval of the Minister of Industries, Production and Special Incentives. Recruitment of staff in corporations and units is often on a permanent basis, while personnel in professional and technical cadres are mostly appointed "on contract, through secondment from the government, and by the re-employment of retired government and military officers" (ibid).
Financing: Public Industries do not receive any special tax exemptions from the GoP, however they are allowed to borrow from domestic and international sources. The federal government is the underwriter of the repayment of all foreign and some local borrowings. If the enterprise defaults in loan repayments, GoP sometimes intervenes and converts debt into government equity to assist the SOE. The surplus generated by corporations are retained and re-invested in new projects, existing endeavors and/or used for lending purposes. Public limited companies also disburse dividends to their shareholders from the generated surplus.
Extent of Autonomy: Although direct control is often "exercised by the ministerial appointment of members of the board of directors" (p.3), the extent of ministerial control in every day operations of companies is negligible. The Minister for Industries, Production and Special Incentives is however answerable to the Parliament for not only the policy but also the operations of its companies.

Source: ASOSAI, 1989

3.1.5 Current Pace of the Privatization Programme

Although the pace of privatization was fast between 1991 and 1992 when the government privatized 69 manufacturing units, it became slow in the years to follow given a turbulent political environment. Consequently, only 21 additional manufacturing units could be privatized up till 2000 (Kemal, 2000). Nevertheless, the military coup leader of 1999, who was candidly briefed by the IMF regarding the necessary criteria to qualify for the PRGF – privatization being part and parcel of it – took a sharply biased policy stance towards privatization (Khan, 2003; Ghausi 2006b), which resulted in the institution of a new Ministry of Privatization and Investment as well as the promulgation of PC Ordinance 2000 (Annex-B). This Ordinance gave greater autonomy, clarity and powers to the body (PC, 2006f). Today, the GoP which has made privatization the cornerstone of economic reform (PC, 2006g), is reaping the fruits of previous efforts and is being credited with picking up the speed of privatization from a "jog to a sprint" (Borthwick, 2006: 3).

Since 1991 to date, the total number of privatized transactions in Pakistan has been 160 of which 102 (excluding newspapers) were those involving manufacturing units (Table-3.1). A total of 11 industrial units, comprising of the strategic Pakistan Steel (sale of which has recently been annulled by the Supreme Court), Pak-American Fertilizers and Pak Saudi Fertilizers, have been privatized between 2002 and April 2006 (PC, 2006d). Furthermore, there are a total of 40 SOEs

(excluding Pakistan Steel) still waiting to be privatized, of which 20 are on the active list of privatization scheduled for the current financial year (Ziauddin, 2006). This list is inclusive of nine big and small manufacturing units (PC, 2006e).

Table 3.1 – Number of Privatized Transactions in Pakistan between 1991 to 2006 (April)

Sector	Number of Transactions	Amount (Millions of Rupees)
Capital Market Transaction	18	31,684
Banking	7	41,023
Energy	14	57,559
Telecom	4	186,058
Tourism	4	1,805
Automobile	7	1,102
Cement	16	11,860
Chemical / Fertilizer	22	40,465
Engineering	8	21,866
Ghee Mills	23	846
Rice/Roti (bread) Plants	23	328
Textile	3	215
Newspapers	5	270
Others	6	160
Total	**160**	**395,241**

Source: PC, 2006b

3.2 Pakistan's Privatization Programme

The privatization programme of Pakistan builds on the perception that the government has no business running business (Shaikh, 2003). The PC's official website details an array of reasons justifying the need to privatize in Pakistan. These include amongst others, an understanding that SOEs exhibit characteristics of "(m)ismanagement and overstaffing", and are "(i)nappropriate and costly investments" providing "(p)oor quality and coverage of services", running "(h)igh debt and fiscal losses and generating (p)roduction and profits … well below … potential" (PC, 2006a: 1). The public sector is viewed to have "failed to deliver" (ibid) and it is through privatization that the aims of "strengthening public finances and bringing in new investment while simultaneously enhancing the quantity and quality of goods and services" can be achieved (PC, op. cit. p.2). "By attracting better management and staff and by freeing the company from public sector red tape and procedures", GoP believes that "privatisation can unleash the potential of the company" (ibid). In addition, it is reasoned that the "greater efficiency and availability of capital, coupled with built-in incentives to improve customer service, will result in more satisfied customers and a lowered need to raise taxes" (ibid). Clearly, the neo-liberal case for privatization discussed in the earlier chapter forms the ideological underpinnings for the rationale behind Pakistan's privatization programme.

Nonetheless, in order to understand whether this rationale is justified in the light of empirical data or not, it is imperative that first an understanding of the objectives, technique and process of privatization in Pakistan is achieved.

3.2.1 Objectives

According to Kemal (2000), the mission of the PC from 1988-90 was to "divest 14 loss making manufacturing units and raise funds by selling shares of profit making units for retiring public debt and thus reducing debt servicing (costs)" (p.144). Other broad mission statements followed in subsequent

years, but it was after the PC Ordinance 2000 that a defined set of objectives surfaced, which continue to be the guiding principles of privatization today. These include:

- Enhancing the quantity and quality of goods and services
- Strengthening GoP's fiscal position through using 90% of proceeds to retire debt, and stemming fiscal bleeding from loss-making SOEs
- Broadening and deepening capital markets
- Reducing opportunities for corruption
- Generating productive employment (Shaikh, 2003; PC, 2006a)

3.2.2 Methods

Although various governments have used different methods of privatization (Table-3.2), divestiture through auction comprising open bidding for small and medium industrial units and sealed bidding for larger enterprises, has been the primary mode of privatization (PES, 2005).

3.3.3 Process

Privatization in Pakistan is primarily a seven step process, which is tailored for cases of capital market transaction and cases of divestitures through auction. Nonetheless, common and major steps include identifying the list of potential SOEs for privatization, hiring the Financial Advisor (if required), carrying out financial, legal and technical due diligence, identifying and instituting required sectoral or regulatory reforms, valuating property, conducting the bidding process, approving (or rejecting) the bid, receiving receipts, handing over the business and officially publishing the summary of the transaction (Box 3.2).

Table 3.2 Key Modes of Privatization Used in Pakistan

Method	Features
Third Party Sales – Auction	Primary method used
Public Offering	Rare for manufacturing industries
Third Party Sale to Employee's Management Groups	Handover takes place on the basis of an evaluation of assets, liabilities and net worth and if the maximum bid received is matched Took place for some cement, ghee, engineering, automobile and chemical units
Sale to modaraba companies	These companies work on the Islamic profit-and-loss sharing principle
Management contracts with modaraba companies	Leasing or contracting of management for a specified period Specific to the Service industry
Lease management contract with the workers for a specified period	Assists management groups to ultimately buy out the enterprises

Source: Kemal (2000)

Box 3.2 The Privatization Process

The Identification Stage – During this stage, a list of potential SOEs for privatization, prepared in consultation with the concerned ministry, is submitted to the Privatization Board for endorsement and subsequently forwarded to the CCoP for approval.
Hiring of a Financial Advisor – A requirement only for major transactions, the hiring of a Financial Advisor is carried out through the invitation of EOI and subsequent evaluation of technical proposals.
Due Diligence – Legal, technical, and financial due diligence, which involves the identification of legal problems, evaluation of asset condition and examination of company accounts, is carried out for most small and medium industrial units through in-house staff or sub-contracted firms. In case of major transactions however, the Financial Advisor assumes this responsibility, identifies the company's reserve value, and subsequently finalizes the privatisation plan, which may include recommendations for restructuring.
Enacting any Needed Regulatory and Sectoral Reforms – Identification of the need to enact or circumscribe any regulatory and sectoral reforms necessary to ensure maximum realization of privatization proceeds is yet another facet of the process. This may include rules specifying the competitive framework, regulatory mechanisms, prices, tariffs, standards, and penalties etc.
Valuation of Property – Either the Financial Advisor or an external firm carries out the valuation of property through a combination (or not) of the discounted cash flow, market value, and/or stock market valuation method.
Pre-bid and Bid Process – EOI for bidding are usually invited through media advertisements. Those who fulfil the criteria of potential bidders are handed over the RFP package containing relevant pre-qualification documents. SOQs are then submitted by interested parties, on approval of which they are given a chance to personally conduct due diligence. A pre-bid conference is also held to clarify any further ambiguities.
Post-bid Matters – After the highest bidder has been identified, the Board of the PC recommends the CCoP whether to accept or reject the bid value. Upon approval, a letter of acceptance/intent is issued to the party, following which the sale purchase agreement is finalized, sale proceeds are collected and the property is transferred. Recently, the policy of payment has been changed to upfront rather than deferred, which was the norm of earlier transactions. Finally, within 30 days of transaction, the PC publishes a summary of the process in an official gazette which is available online.

Source: PC, 2006c

3.3 Industrial Privatization in Pakistan – A Micro and Macro-Level Analysis

Was the public sector manufacturing industry as inefficient as it is perceived? Has the privatization programme really delivered its targeted goals? Have the effects of this programme been largely positive on the micro and macro levels? Answers to these questions can be achieved through an analysis of the performance of public sector manufacturing industries, the performance of those units which have been privatized and the wider social and economic consequences of the privatization programme. The theoretical framework established in the previous chapter shall guide the following analysis.

3.3.1 Micro-level Analysis

Empirical studies of Naqvi *et al* (1991), Kemal (2000) and Khan (2003) draw interesting and eye-opening conclusions regarding the perceived allocative and productive inefficiency of the public sector as against the private sector.

3.3.1.1 Incentives and Efficiency

Naqvi *et al* (1991) in a study of the public sector large-scale manufacturing industry of Pakistan during 1987-88 conclude that in "five out of eight corporations(,) the average rate of return on capital exceed(ed) (in 1987-88) the maximum rate of interest on public debt instruments" (p.122). This indicates not only profitability but could also points to an increase in the fiscal burden following privatization of the units of these

corporations. Furthermore, "in two out of three industries where both the private and the public sectors operate(d) simultaneously and produce(d) similar goods, the pre-tax return on equity of the public sector units …(was)… significantly higher than that …(of)…private sector units" (p.114).

The more recent performance of public sector manufacturing industries, despite continued privatization and change in measurement criteria for the production value of the years 2004-05 & 2005-06, has also been noticeable. Although the performance is expected to witness a downfall in the year 2005-06, the indicators of production value, taxes & duties, net sales and pre-tax profits show an increasing trend between 2001 and 2005 (Figure-3.1). Similarly, the percentage change in the performance indicator of production value per year also shows an increasing positive trend up till 2003-05. Pre-tax profits register a positive increasing trend up till 2002-04, but show a decreasing though positive trend in 2003-05 (Figure-3.2). Nevertheless, a decreasing yet positive trend continues to be maintained up till 2003-05 for all indicators after which a negative trend follows (PES 2003; 2005; 2006). All in all, contrary to the popular belief, the performance of public sector manufacturing industries continues to be anything but dismal.

In the defence of those units that are loss-making, Naqvi *et al* (1991) insist that those costs of public industries, which are associated with fulfilling social objectives, also need to be taken into account while assessing performance because these are embedded in the production cost structure of some public sector firms. They estimate a 5% employment cost and a 10% higher production cost for industries located in backward areas. On account of protectionism, non-competitive functioning and resultant allocative inefficiency, they categorically stress that except for Pakistan Steel, which is the only kind of its industry in the public sector having no domestic public or private competition of its level (except for a few product categories and future competition from Al-Tuwairiqi Steel Mills), all other public industrial units compete not only amongst themselves but also with the private sector. The authors admit that umbrella corporations determined pricing policies for some units; however they deny the accusation that public sector industries enjoyed greater protection than the private sector. In fact, they show that during 1987-88, the average rate of effective protection[2] "for industries in which public sector … participated … (was)…only 39 percent…" as against 70 percent for industries dominated by the private sector (p.116).

Regarding managerial incentives, the authors insist that not only was performance of public sector industries evaluated according to a performance signalling system by the EAC, the associated rewards disbursed to the workers and management were independent of the corporation and given at the unit level, thereby stimulating greater incentives for efficiency.

In the case of private sector, Siddiqui (2004a) shows that the incentives for the *rational and maximizing* private buyers in five of the six engineering units privatized between 1992 and 1996 were not enough to ensure that viable concerns remained, at the least, going concerns (Box-3.3). He also claims that the private sector in some cases was simply interested in purchasing assets, especially real estate and never had the intention of profitably running these entities. This was the case of the Textile Machinery Company, whose buyers allegedly sold individual plant machinery items of this unit. A similar story is told of Zeal Pak Cement, whose buyers also stripped the company of its assets (Khan, 2003) (Table-3.3).

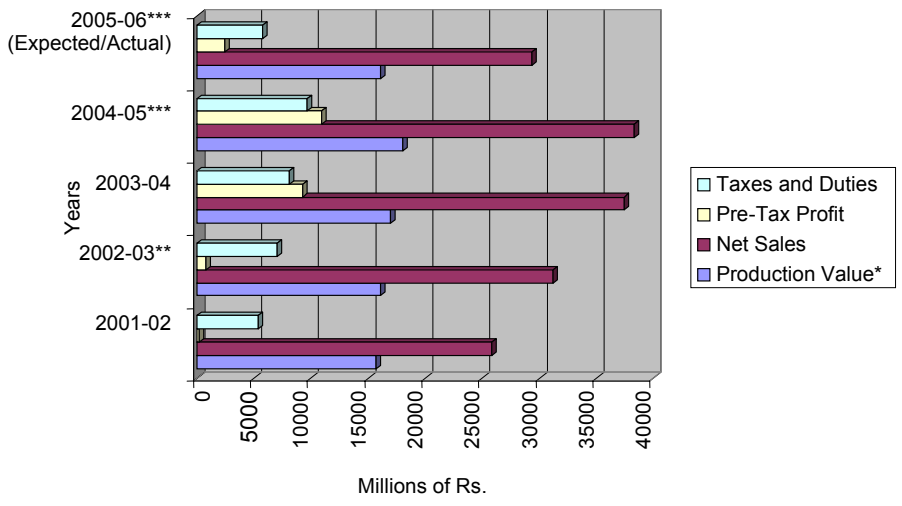
3.3.1.2 Ownership and Efficiency

Kemal (2000) in his study on the performance of the manufacturing sector after the privatization of 69 units in 1991-92, concludes that "(t)he analysis of variance does not show any difference in the growth rate of output in the pre and post-privatization period" (p.164); pre-privatization being the period between 1986 and 1991 while post-privatization being that between 1992 and 1997. At the privatized industry level, he concludes that the post-privatization growth rate out of a total of 14 industries fell for three, increased for two and remained unchanged for nine industries. Similarly, he also shows no change in the indicators of return to equity and return to fixed assets[3] during both periods but cites a

decline of 6% in TFP of the manufacturing sector.

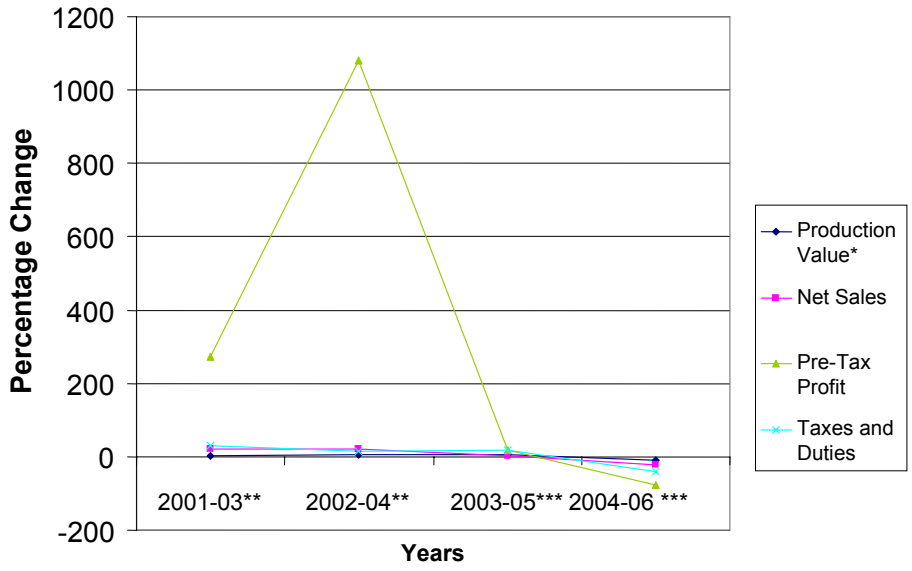
Complementary statistics are also quoted by Khan (2003) who cites the results of the Asian Development Bank's 1998 report on the "Impact and Analysis of Privatization in Pakistan" (p.5) and shows that out of a sample of 65 privatized public manufacturing enterprises (including Ghee (edible oil) and Rice Mills), performance-wise 13 units were better off, 25 remained the same while 27 were worse off than before. Furthermore, Siddiqui (2004a) citing the EAC report of 2000-01 titled "Dis-investment of Manufacturing Enterprises in Pakistan - Performance Review", also notes that "there was a significant decline in manufacturing activity at the national level when comparing operating results of … 61 privatized units during pre- and post privatization periods" (p.3). He further claims that out of the 61 privatized units, approximately 93% were operational at the time of privatization, however subsequently at least 50% either closed down or were liquidated following privatization.

Figure 3.1 Performance of Public Sector Industries Between 2001 and 2006



Source: PES, 2003, 2005, 2006
* At constant prices of 1992-93
** Actual for 8 months (July- Feb.) and estimated for 4 months (Mar-Jun)
*** Production value of PACO is at current prices. NFC & Pak Steel is at constant prices of 1999-2000 while SEC at 1992-93

Figure 3.2 % Change in Performance Indicators of Public Sector Industries Between 2001 & 2006



Source: PES, 2003, 2005, 2006
* At constant prices of 1992-93
** For year 2002-03, actual for 8 months (July- Feb.) and estimated for 4 months (Mar-June)
*** For years 2004-05 and 2005-06, production value of PACO is at current prices. NFC & Pak Steel is at constant prices of 1999-2000 while SEC at 1992-93

Table 3.3 Some of the Industrial Units Privatized Between 1991 and 1997 that Subsequently Shutdown

Sr	Name	Industrial Category	Year of Privatization	Buyer(s)
1	Naya Daur Motors	Automobile	Jan-93	Farid Tawakkal & Saleem I. Kapoorwala
2	Dandot Cement	Cement	May-92	Employee Management Group
3	Zeal Pak Cement	Cement	Oct-92	Sardar M. Ashraf D. Baluch
4	National Cement	Cement	Jan-95	Employee Management Group
5	General Refractories	Cement	Feb-96	Shah Rukh Engineering
6	Pak PVC	Chemical	Jun-92	Riaz Shaffi Reysheem
7	Swat Elutriation	Chemical	Dec-94	Sahib Sultan Enterprises
8	Nowshera PVC	Chemical	Feb-95	Al-Syed Enterprises
9	Nowshera Chemicals	Chemical	Apr-96	Mehboob Ali Manjee
10	Pak China Fertilizer	Fertilizer	May-92	Schon Group
11	Karachi Pipe Mills	Engineering	Jan-92	Jamal Pipe Industries
12	Metropolitan Steel	Engineering	May-92	Sardar M. Ashraf D. Baluch
13	Pak Switchgear	Engineering	Jun-92	Employee Management Group
14	Quality Steel	Engineering	Apr-93	Marketing Enterprises
15	Indus Steel Pipe	Engineering	Jul-97	Hussien Industries
16	Textile Machinery Company	Engineering	Oct-95	Mehran Industries
17	Fazal Vegetable Ghee	Ghee	Sep-91	Mian Mohammad Shah
18	Haripur Vegetable Oil	Ghee	Jul-92	Malik Naseer & Assoc.
19	Khyber Vegetable	Ghee	Jan-93	Haji A. Majid & Co.
20	Suraj Ghee Industries	Ghee	Jan-93	Trade Lines
21	Hydari Vegetable Ghee	Ghee	Aug-92	Employee Management Group
22	Quaidabad Woollen Mills	Textile	Jan-93	Jehingir Awan Associates

Source: Khan, 2003; Siddiqui, 2004a; PC, 2006d

Box 3.3 Failed Privatization of Light Engineering Units

Between 1992 and 1995, the GoP privatized six light public sector engineering units, five of which subsequently shutdown. These industrial units were privatized at a total price of Rs.140 million while the revised sale price for some units was even less than the bid value. Moreover, the GoP picked up all liabilities and relieved employees under the VSS before handing over the units to private hands. A brief account of each of these units is given below.

Karachi Pipe Mills: Established in 1955, Karachi Pipe Mills was annexed to the public sector following nationalization in 1972. At that time, it was the only API approved "manufacturing facility and its products enjoyed a high reputation in the market" (p.5). The production and sales of this unit during the period 1985-86 to 1987-88, were in the range of 11,000 to 14,000 tons of finished goods. Pretax profit amounted to Rs.3 million and Rs.4.8 million in the years 1985-86 and 1987-88 respectively, but the company suffered losses in subsequent years because it was on the list of active privatization; however profits were again earned during the year 1990-91. Nevertheless, the company was privatized in 1992, and registered pretax losses of Rs.9 million and Rs.7 million in the years 1992-93 and 1993-94 respectively. The factory subsequently closed its operations in 1995.

Pioneer Steel Mills: Nationalized in 1972, Pioneer Steel Mills was established in the private sector in 1962. As a public sector unit, the company incurred losses during most of the pre-privatization period. GoP sold Pioneer Steel Mills at a revised sale price of Rs.4 million to its previous owner in 1992 and also extended a loan/advance to the company worth Rs.55.4 million. The management of the company did not repay any part of this loan (at least up till the published date of the source), which had increased to Rs.161.5 million as on 31.5.2000. "The company is in operation, but no data regarding its production, sales, profit/loss, etc. during the post-privatization period is available either with the PC or MoIPSI" (p.5&6).

Metropolitan Steel Corporation: Metropolitan Steel Corporation was established in 1965 at Karachi and was nationalized in the 1970s. The company had both a national and international reputation in steel products. Although during late 1980s, production & sales and pre-tax profit were in the range of 80,000 tons of finished goods and between Rs.20 million to Rs.45 million respectively, the listing of the company on active privatization led to a performance decline after 1989. Following privatization in 1992, the management of the company changed a number of hands, yet production dropped to Rs.480 million in 1992-93 as compared to Rs.731 million during the year 1990-91. A spiral decline in the performance forced the closure of the company in the year 2000.

Pakistan Switchgear: GoP purchased Pakistan Switchgear from Wazir Ali Group in 1975. An important supplier to the power industry, this company was sold in 1992 under the employee's buy-out scheme. The factory has remained closed ever since.

Quality Steel Works: Established in 1954 and subsequently nationalized in the 1970s, Quality Steel Works boasted an output of 28,000 tons of finished goods and pre-tax profit worth Rs.13.8 million during 1987-88. The company remained in profits until it was offered for sale in 1990-91. After privatization in 1993, production and sales declined to Rs.152 million and Rs.181 million during the year 1996-97 as compared to Rs.277 million and Rs.264 million, respectively, in the year 1989-90. The unit was closed in 1998.

Textile Machinery Company: GoP setup the Textile Machinery Company in 1975 at a cost of Rs.18 million. "The company earned pre-tax profit of Rs.7 million, 6 million and 3 million, during the financial years 1985-86, 1986-87 and 1987-88, respectively, though it hardly operated at 50 per cent capacity utilization" (p.7). Since its privatization in 1995 however, operations are at a standstill and the buyers have allegedly stripped and sold individual items of plant machinery.

Source: Siddiqui, 2004a

3.3.1.3 Monitoring & Accountability and Efficiency

Public offerings as a form of privatization in Pakistan have been modest, while complete divestiture through capital market transactions has been rare, especially in manufacturing industries. Of the Rs.395,241 million (US$6,636 million[4]) collected as total

privatization receipts to date, merely 8.1% has been received through capital market transactions (PC, 2006b). Moreover, the stock markets of the country are volatile and public confidence to invest in them is low (Dawn, 2006a). Matters are made worse with stock market crashes such as the one in March, 2005 and more recently in April-May, 2006, when a few stock brokers gained significantly at the expense of small investors (Dawn, op. cit.).

Therefore, even if the government divests its majority stake (or some amount of shares along with management control) in a public limited company to a single buyer (or consortium of buyers) through auction, the underlying structure of ownership remains largely unchanged. This scenario points at the high level of unlikelihood for improved (if any) monitoring benefits arising from stakeholder pressure. Accountability on the other hand is far more problematic, given that a good number of running businesses have been shutdown by private buyers without the consent of the very taxpayers whose money was used to establish and run those firms. With a virtually non-existent feed-back mechanism of the PC regarding privatized units and inconsistency in imposing penalties upon breach of often ill-devised inconsistent agreements (Siddiqui, 2006d), accountability of privatized entities is left to the questionable discipline of the markets.

3.3.1.4 Political Interference and Efficiency

Corruption in public enterprises, which the privatization policy of the government aims at curbing, is a problem that has pervaded the entire process of privatization in Pakistan. At least three of the Chairmen of PC in the 1990s were jailed on different charges and accounts (Ghausi, 2006b). In 2002, the Public Accounts Committee also questioned the then Secretary of the Privatization Commission about a sum of Rs.80 billion which could not be traced under the debt retirement head, where this amount should have legally been directed to (Klasra, 2002).

More recently, the sale of Pakistan Steel to a consortium of the Saudi Al-Tuwairiqi Group of Companies, the Russian Magnitogorsk Iron and Steel Works and the Pakistani Arif Habib Group of Companies, at a modest US$362 million given that the value of just its assets was about US$5 billion (Siddiqui, 2006c), is being considered as the worst form of patronage extended by the government. The Acting Minister is being accused of by-passing the CCoP in hastily deciding to sell the company to the bidders without proper approval (Ghausi, 2006b).

Illegal activities are not limited to the government and extend deeply in the private sector, which indulges in unlawful tactics to ensure maximum gain. Again, Pakistan Steel is the prime example of how the Russian Magnitogorsk Iron and Steel Works joined hands with the consortium of the Saudi Al-Tuwairiqi Group of Companies and the Pakistani Arif Habib Group of Companies on the day of the bidding, which is against the rules of competition and was pronounced as one of the reasons for the annulment of the sale of Pakistan Steel (Iqbal, 2006b)

On the issue of political appointments of incompetent managers, across the board generalizations cannot be made, especially when the examples of successful turnarounds such as those of Heavy Mechanical Complex (Box 3.4), Heavy Electrical Complex (Box 3.5) and Pakistan Steel are reviewed, which still remain in state hands. It is true that Pakistan Steel is being headed by an army officer who was the President's political appointee, yet the achievements of the management and workers, who uplifted the loss making giant into a profitable venture, speak of nothing more than the competence of everyone involved. In 2004-05, Pakistan Steel achieved "record production levels, sales and profits…(which)…enabled the company to invest more and reduce debt, (that ultimately led to the)…lowering …(of)…interest payments to the banks" (Borthwick, 2006: 1).

Box 3.4 Future of the National Flagship of Pakistan's Engineering Industries

Setup in the 1970's with the economic and technical assistance of the Chinese, HMC is the largest heavy engineering product design facility in the Pakistan. Consisting of the Heavy Mechanical Works and Heavy Foundry and Forge Works, this complex has a paid up capital of Rs.1,077 million and is incorporated as a private limited company which is wholly owned by the GoP. The production facilities of the complex include light, medium and heavy fabrication, light, medium and heavy machining and assembly, steel foundry, cast iron foundry, non-ferrous foundry, light, medium and heavy forging, heat treatment, surface treatment, galvanizing, woodworking, die and tool room and other infrastructure.

Having been the leading national engineering industrial unit of the country for almost five decades, the complex is attributed with successfully developing new products for strategic and defence industries, employing thousands of workers and training hundreds of engineers and technicians. No other domestic engineering company can boast a similar distinction of the way HMC has placed Pakistan on the map of global exports. Besides exporting engineering products to Bangladesh, Afghanistan, Sri Lanka, Ghana, Uganda, Kenya and the UAE, the complex has setup turnkey mills and plants of sugar and cement in Indonesia and Bangladesh.

A profitable complex that saved Pakistan billions of dollars worth of import bills, HMC saw its demise in the 1990's, when poor investment climate and slow industrial development in the country led to the gross under-utilization of its estimated 35,000 tons per year production capacity. Following heavy losses and high burden of debt servicing, various governments undertook restructuring measures, which could not materialize due to inconsistent policies and lack of commitment to run the complex as a state-owned entity. Consequently, HMC was put on the list of privatization in 1996, after which heavy staff downsizing through VSSs was witnessed. Furthermore, the GoP also withdrew fiscal concessions and policy support for indigenization, which was one of the major objectives of HMC's functioning.

Despite all odds, however, HMC has managed to gain stability in both financial and commercial terms. It achieved sales worth Rs.1,403 million during the year ending 30th June 2005 compared to Rs.515 million in 2002-03 and earned gross and operating profits worth Rs.189 and Rs.66 million respectively. The complex has secured orders worth Rs.2,927 million which have improved the cash flow position and allowed HMC to repay part of its loans, which stood at Rs.409 million compared to Rs.878 million in the year 2001-02.

Although the future for the products and services of HMC in the domestic and international markets seems bright, the complex is still sitting on the active list of privatization scheduled to take place in the year 2006. It is unfortunate that Pakistan has not learnt from the likes of France when it comes to saving national champions, who continues to bail out troubled state-owned enterprises which are operative in competitive global markets.

Source: Siddiqui, 2006a; Economist, 2004

Box 3.5 The Heavy Electrical Complex: A Restructuring Success Story

HEC, established in 1994 at a cost of Rs.1,158 million with the economic and technical assistance of China, is a one of its kind factory with the largest integrated facility for engineering, production and testing in the country. The complex, which was the brain child of PIDC, has an installed capacity of producing 148 Nos. power transformers and 66 kV electricity transmission systems. It was the importance of power transformers as a vital link in power transmission and distribution systems that essentially fuelled the idea of establishing this complex.

Unfortunately, the start up phase of the factory was not impressive because it failed to secure the domestic market for its products, which was being served by imports. Reasons behind this failure can be credited to the vested interests of multinationals and their lobbyists in Pakistan, whose own interests would have been compromised if self-reliance in the electrical capital goods industry serving the power sub-sector would have been achieved. The result nevertheless was a gross under-utilization of HEC's productive capacity. Given that the government had not provided it with any working capital, the cash-starved company borrowed loans from commercial banks and ultimately defaulted on not only them but also the Chinese and Swiss credits utilized earlier for plant machinery purchase. Subsequent attempts to privatize the company also failed and this dismal state of affairs continued till the year 2002.

Today, HEC has posted profits and has orders worth Rs.757 million for the manufacturing and supply of transformers in addition to the Rs.52 million for the repair and rehabilitation of old power transformers. This achievement came as a result of the management's concerted marketing efforts, financial restructuring and the government's assistance in picking up loans worth Rs.620 million (app). The company has also serviced Rs.70 million worth of commercial bank loans through its own resources. Overheads are minimal with only 50 employees out of a total of 380 being permanent. Moreover, there happens to be no labour union, housing facility or a major welfare scheme for the employees either.

With a growing demand in the power sector, the future for HEC products looks bright. However, the company will need further investment in plant modernization, technological improvement and in-house testing facilities if it wishes to maintain market leadership. Given the failed privatization of many engineering units and the special nature and needs of heavy industries, the future for HEC itself looks uncertain, as it sits on the list of nine manufacturing units scheduled for privatization in 2006.

Source: Siddiqui, 2006b

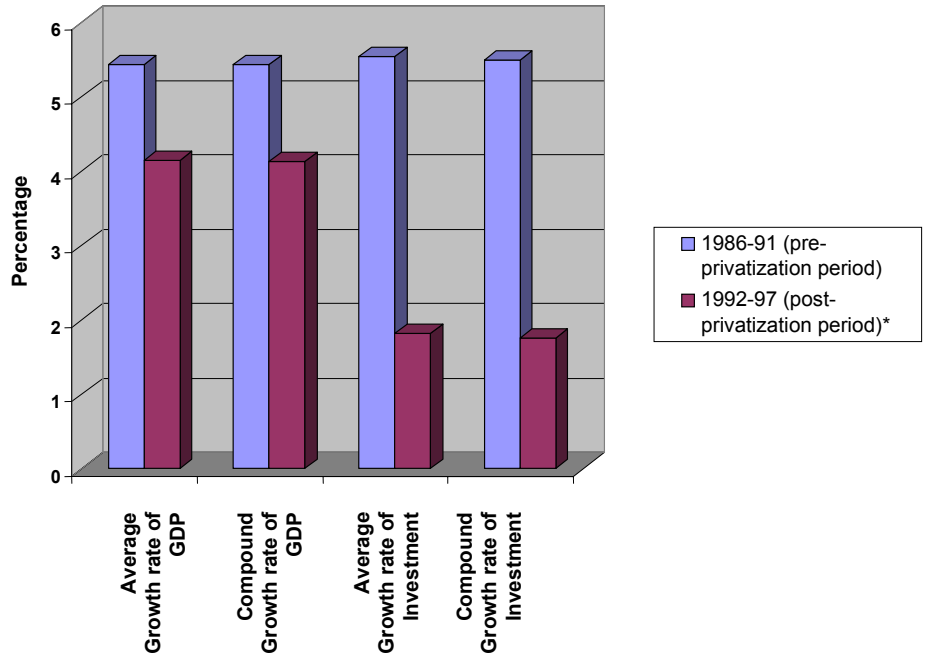
3.3.2 Macro-Level Analysis

The macro-economic analysis of the consequences of manufacturing industry privatization and privatization as a whole also gives ample evidence on the generally negative impact of this policy instrument in Pakistan.

3.3.2.1 Economic Growth and Performance

The argument of economic growth and performance improvements due to privatization is carefully refuted by Kemal (2000), who shows that the average and compound growth rates of GDP declined by 1.29% and 1.31% respectively in the post-privatization period. Even the average and compound growth rates of investment fell by 3.73% respectively (Figure-3.3). In the manufacturing sector, average growth rate of output fell from 3.85% to 3.45% while the compound growth rate fell from 6.03% to 2.16%[5] (Figure 3.4). Accepting the possibility that these reductions may have been the result of IMF's deflationary stabilization programmes, which were being implemented over the same period, he argues that privatization still had some part to play in the decline, but does not show how.

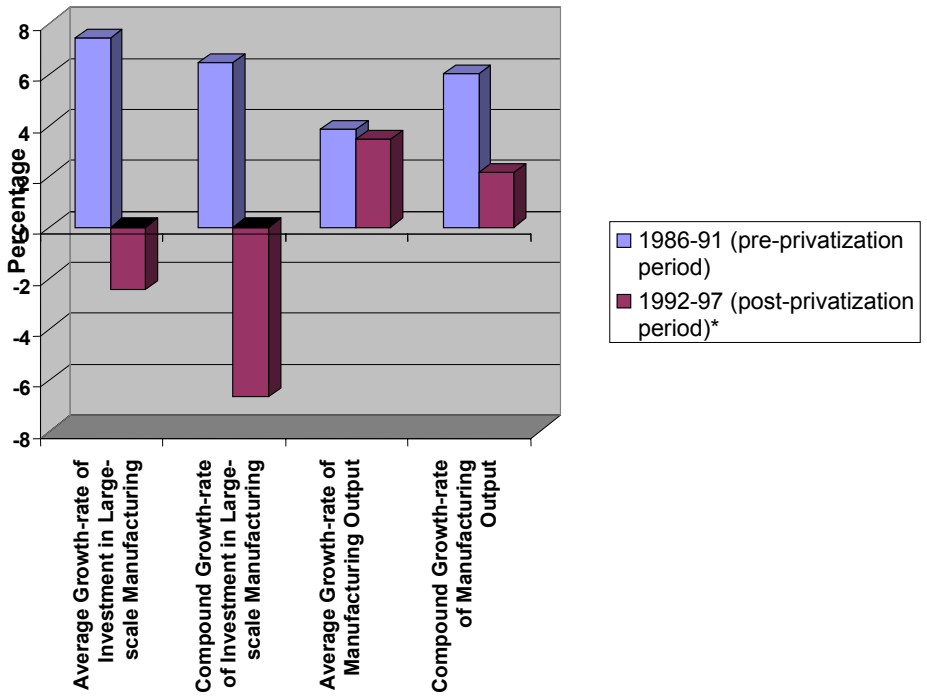
Figure 3.3 Macro Indicators of Pre and Post Privatization Scenario (1986-97)



Source: Kemal, 2000
* The year 1991-92 is excluded as the year of privatization

On the other hand, the share of the manufacturing industry in Pakistan's GDP, although on the rise between 1999 and 2005, has never been as significant as that of agriculture or the services sector (PES, 2005) (Figure-3.5) The public manufacturing sector, which forms an even smaller part, has fetched to date privatization receipts of Rs.7.66 billion[6], which in the face of Pakistan's massive external debt that stands today at US$ 36.5 billion (figure for end March; PES, 2006) (Figure-3.6) would account for a mere 1.8%[7] debt reduction, if it is assumed that 90% of these receipts shall be utilized for the cause[8]. Of course, the related expenditures of the PC, restructuring costs and the money that is returned to the SOEs will also be deducted from this amount, ultimately leaving very little for the cause of debt retirement. 10% of the total, which is supposedly earmarked for poverty alleviation programmes, becomes even more insignificant to bring about tangible results in poverty reduction. The insignificant value of privatization receipts can simply be judged from the fact that Pakistan Steel alone paid taxes and duties worth Rs.8.67 billion to the government in the year 2004-05 (PES, op. cit.).

Figure 3.4 Investment in and Output of the Manufacturing Sector Pre and Post Privatization (1986-1997)



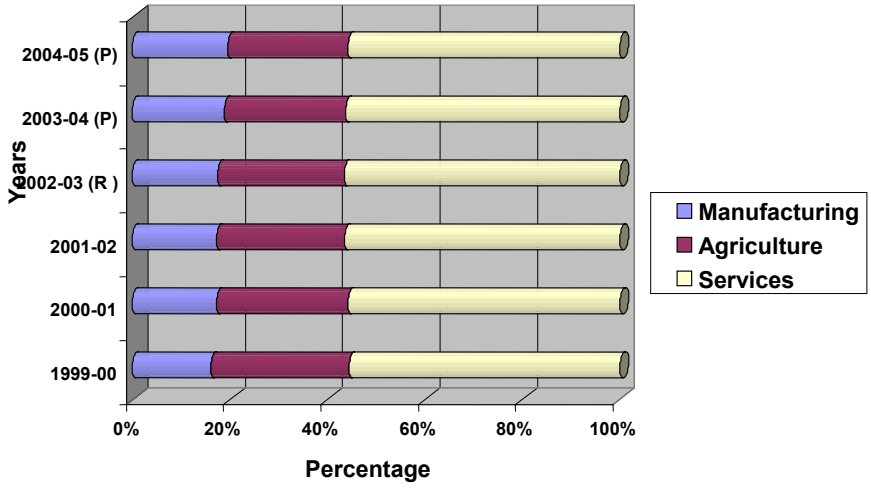
Source: Kemal, 2000

With reference to reduction in budget deficits, Naqvi *et al* (1991) argue that "even if the government divest(ed) all the industrial enterprises it owns, the reduction in budgetary deficit from this source … (would) … not exceed 0.6% of the GDP (figures for 1987-88)" (p.120). Furthermore, the receipts from privatization have also often come at a net loss to the government. This was the case of Karachi Pipe Mills, Pioneer Steel Mills and Pakistan Switchgear, where the revised sale price was not only less than the reserve value determined by the PC, but also less than the initial bid value (Siddiqui, 2004a).

Direct subsidies in the manufacturing sector have only been extended to the fertilizer sector in the past, while the government does assist in picking up some loans or simply converts markup into equity for loss making units (Siddiqui, 2006d). There will obviously be an improvement in the post-privatization fiscal health of the state, however the extent of this improvement remains contingent upon the value of benefits (such as tax leverages) extended to the buyers and the value of liabilities that the government agrees to pick up. For instance, GoP agreed to sell Pakistan Steel for Rs.2.15 billion[9] while it simultaneously picked up liabilities and extended benefits worth Rs.18 billion and additionally committed to worker compensation worth Rs.15 billion (Iqbal,

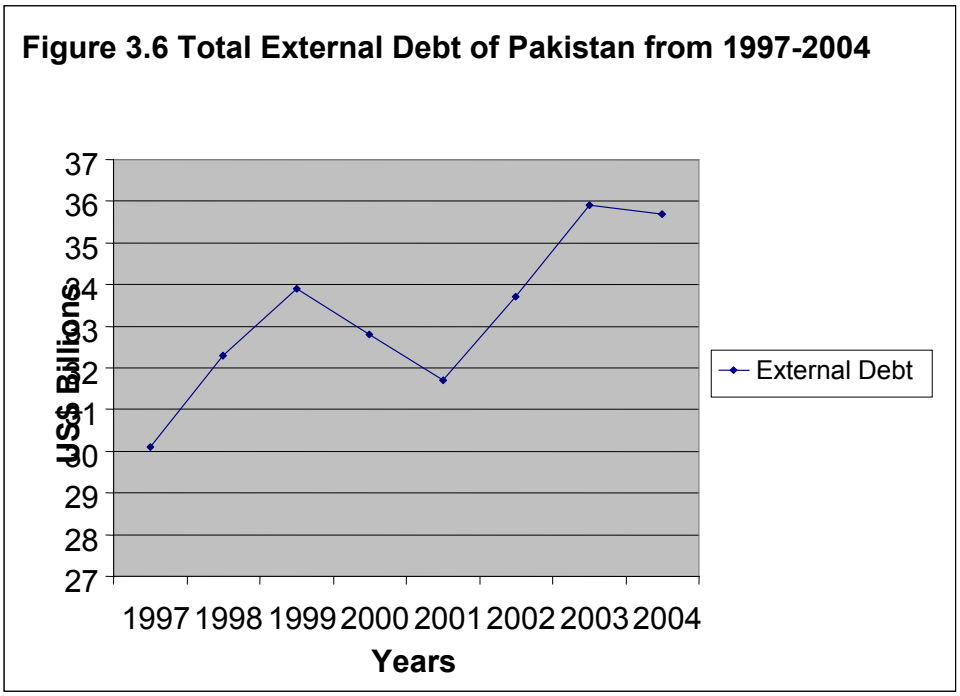
2006b), which reflects the potentially negative rather than positive fiscal impact of privatization. Secondly, the government must also account for the loss of revenue resulting from failed privatizations. For instance, the total duties and taxes paid to GoP by five light engineering units that were shutdown after privatization amounted to Rs.143 million in 1990-91 (pre-privatization period) which is a direct fiscal loss to the government (Siddiqui, 2004a).

Figure 3.5 Sectoral Share in GDP between 1999 and 2005



Source: PES, 2005
P = Projected, R = Revised

Figure 3.6 Total External Debt of Pakistan from 1997-2004



Source: World Bank, 2006

3.3.2.2 Distribution of Assets and Wealth

Dr. Ishrat Hussain, former Governor of the State Bank of Pakistan, described the political economy of Pakistan (before his appointment) as the capture of "an elitist class of civil servants, landlords, merchant capitalists of big industries and big businesses, military officers and elected politicians" (Hussain, 1999 cited in Srinivasan, 2003: 10). In such a society, given that the focus of privatization remains on auction sales to a single or consortium of buyers, the problem of elite capture is progressively perpetuating. According to Rehman (1998), "industry and its associated wealth has become increasingly concentrated in the hands of a few wealthy families … (to the effect that) the industrial assets of the top forty-four business groups are equal to the size of the country's entire national budget" (cited in TI, 2003: 21). Moreover, in a country "where per capita incomes are low and the workers have hardly any savings", the privatization objective of broad-basing equity through public offerings may not be achieved, because "even if … (workers) do buy the stocks, …(they) will do so … to earn … quick profits by transferring these to the richer stock-holders" (Naqvi *et al*, 1991: 121). Such acts will surely promote further wealth and asset concentration.

Other examples of wealth concentration can be traced in the 1990's, when Mian Mansha, a prominent industrialist, emerged as "one of the biggest players in the privatization game"' (Ghausi, 2006b: 2). Today, he along with his extended family enjoys a "monopolistic position in cement production in the Northern Area (of Pakistan)" (ibid). Similarly, no attention to distributional considerations was paid when multiple industrial units were handed over to the infamous groups of industrialists and their relatives, namely Schon and Tawakkal (Khan, 2003). Elite capture of the society is of course also assisted by the fact that some notable members of Parliament happen to be industrialists as well (TI, 2003). All in all, industrial privatization has helped skew the distribution pattern of assets and wealth in favour of the elites of the country.

3.3.2.3 Foreign Ownership and Industrialization

The latest wave of privatization in Pakistan has seen a conscious effort by the government to attract FDI by "packaging up … companies…(and)…offering them to investors from all over the world" (Borthwick, 2006: 3). Although Pakistan Steel has been the only manufacturing unit offered to a consortium of international and national investors, concerns are already being raised about the immediate price hike that various products of the company experienced within a week of bid acceptance (Siddiqui, 2006c). Such price hikes could adversely affect auxiliary and dependent industries in the manufacturing and construction sectors (Siddiqui op. cit.; Borthwick, 2006). The government is also being criticized for allowing the sale of a company that caters to about one-quarter of the country's steel demand, to a consortium comprising of the Saudi Al-Tawairiqi Group, which has already begun the construction of a Steel Mill in Karachi with a production capacity of one million tonnes. This action could have easily granted Al-Tawairiqi a monopoly status in the domestic steel market (Ghausi, 2006a).

By favouring foreign capitalists over local investors, the government may be attracting one time FDI influx; however, it is simultaneously impeding local private sector development. Moreover, Khan (2006) states that technically, the "foreign purchase of … assets is … not FDI because there is no addition to the capital stock of the country" (p.4). Of course, investments in expansion will account for an addition to capital stock, but the GoP is simply *assuming* that this will happen through foreign ownership. The words of current Chairman, Pakistan Steel are reflective of these assumptions, who said that "…we are selling …(Pakistan Steel)… to private owners, who are actually the steel people. They will invest more money, make it more efficient and more profitable". These requirements cannot be mere suppositions and need to be legally bound in agreements, which certainly did not happen in the case of Pakistan Steel (Siddiqui, 2006d). On the other hand, Khan (op. cit.) questions the logic of selling profitable enterprises for acquiring FDI, given that the corresponding outflow on account of foreign income on equity is substantial and has increased from $1.2 billion in 2004 to $1.6 billion in 2005. According to him, such short-sighted selling would result in "one-time receipts (at the expense of) a life-long liability …" (p 4).

3.3.2.4 Unemployment, Feminization of Workforce and Income Inequality

The work of Kemal (2000) on privatization of the manufacturing sector shows that while real wages increased in 1986-91, they subsequently declined in the post-privatization period of 1992-97. Although there was an overall average increase of 5.1% in wage rates within the privatized large-scale manufacturing industries, the wage rate substantially declined in privatized units of the vegetable ghee, compressed gases and textile machinery industries by 12.3%, 22.3% and 30% respectively. Because, in urban Pakistan, the "link between growth and distributional variables works mainly through employment and income" (Tahir & Ali, 2000: 186), the above-mentioned decline in real wages is suggestive of an increase in income inequality.

With reference to employment, Kemal (op. cit.) adds that in the large-scale manufacturing sector, employment fell by 6.7% between 1990-91 and 1995-96. Siddiqui (2004a) also brings to attention the job loss of at least 3,000 engineers, technicians, skilled workers and other staff members following the post-privatization shutdown of five operational light engineering units. A contingent loss in this regard was that the nation lost experienced units which had served as training facilities for skilled technical manpower in the past (Siddiqui, op. cit.). More recently, the services of 1,500 regular and contract employees of PECO were coercively terminated under the Compulsory Separation Scheme when the PC mishandled privatization of this once profitable unit, forcing its closure in 2002 (Box-3.6) (Siddiqui, 2005b). Before these terminations, at least 3,000 workers had already been laid off under the VSS (Siddiqui, 2004b). Absurd policies of the PC have also led to instances of job loss, such as that in the case of General Refractories Ltd, whose buyers were barred from hiring existing factory workers (Klasra, 2002).

Although APSEWAC and the government signed an agreement in 1991,

which granted workers amongst other benefits, a guaranteed job for the first year of privatization, fears of job insecurity and future uncertainty forced as many as 63.3% of the employees of privatized manufacturing industries in 1991-92 to opt for monetary compensation through the VSS (Kemal, 2000). Some permanent workers were even forced to take the VSS package, only to be re-hired on contractual basis by the company (Kemal, 1999). It is believed that at least 80% of employees who opted for this scheme in all privatized units of the country (including manufacturing) are suffering from joblessness (ActionAid, 2006).

Box 3.6 Nine Failed Attempts to Privatize Pakistan Engineering Company Ltd

PECO is Pakistan's pioneering engineering unit, which was established in 1948 and subsequently nationalized in 1972. The Kot Lakhpat and Badami Bagh Works in Lahore are annexed to this unit. Before the 1990's, PECO branded light engineering products were synonymous to quality and performance, which were competitively priced and economical to operate. It was not until 1990, that the company suffered losses for the first time in its history, following which it was placed on the list of active privatizations. It has been more than 13 years since PECO has been sitting on this list and nine attempts to sell the company between 1991 and 2001 were made by the PC, but to no avail.

In 1991, the PC offered PECO Badami Bagh Works through auction to investors but the response received was unsatisfactory. Later, the PC organized a separate auction of machinery and land of Badami Bagh Works, but did not take affirmative decision on the bids received. In 1993, the ECC of the Cabinet decided to dismantle and transfer the machinery and structure of Badami Bagh to Kot Lakhpat, and subsequently transferred 260-kanal of land to the PC. Following this transfer, the PC divided land into small plots and placed them for auction, however again, none of the bids received were acceptable to the PC.

In 1999, the PC made yet another attempt to auction PECO's assets which included the operational Kot Lakhpat Works and the land of Badami Bagh. Even the appointment of financial advisors and organization of international and national road shows could not compel investors to invest in PECO's assets. Two subsequent futile attempts to sell-off the land of Badami Bagh, and the Kot Lakhpat operations plus Badami Bagh land in January 2001 and August 2001 were again made. In November 2001, the GoP approved a strategy for selling off Badami Bagh land, however the PC did not take affirmative action in this regard. In January 2002, the CCoP decided to closedown the remaining operational units of the company. Only the business of producing transmission towers is currently being run under the banner of PECO.

Unfortunately, these failed privatization attempts of the company destroyed its credibility with network dealers and customers, who were hesitant to take or place orders. Most of the resources of the management were channeled to facilitate the PC in its unsuccessful privatization efforts, which resulted in enormous liquidity problems and heavy losses for PECO that had accumulated to Rs.1,741 million as on 30th June, 2004. Unfortunately, the government or the PC was not interested in taking measures that could have ensured that PECO remained a viable and going concern.

Source: Siddiqui, 2004b, 2005b

Having interviewed a sample of union leaders of privatized units, Kemal (1999) notes that while employee's old age benefits remained intact, the pension scheme for managers and professionals was abandoned, bonuses were slashed and increments to salaries were halted. Citing the Employee's Federation of Pakistan survey of 1993, he further contends that the "fringe benefits in the private sector are lower and workload is higher compared to the public sector" (p.41). These evidences

essentially point to a decline in real earnings. More recently, employees of Pakistan Steel have raised concern that because automation is hampering the pace of employment generation, potential redundancy and unemployment after privatization is becoming increasingly imminent (Borthwick, 2006). Zaidi (2003) also opines that privatization coupled with slow industrial growth especially in manufacturing, has led to a slowdown and possible reversal in formal sector employment, and has prompted an increase in the growth of the informal sector. This trend, along with the post-privatization demise of organised and unionized labour, (Zaidi, op. cit.) points to the growing feminization of labour in Pakistan.

3.3.2.5 Strategic National Interests

Pakistan Steel is considered as the "mother industry" of several other important industries in Pakistan (Ghausi, 2006a). Foreign ownership of such an economically strategic industry may compromise national interests in several ways, one of them being the sale of Pakistani produced steel to the foreign country of origin by essentially by-passing the domestic market (Borthwick, 2006). Furthermore, the company owns 7,520 acres of valuable limestone and dolomite quarries in Thatta District (Siddiqui, 2006c), which could be exploited against national interests by foreign owners.

It is, nonetheless, true that most local owners have proven to be no more "patriotic" than foreign buyers in Pakistan, but this observation strengthens the case for public ownership all the more. However, given the accelerated pace of privatization in the country, critics fear that these buyers (foreign more than local) might even end up selling the country's strategic assets to members of hostile nations, thereby raising sovereignty issues. Such concerns were raised when "Lakshmi Mittal, the Indian-born steel magnate … had shown interest in buying the Magnitogorsk Steel Works, which was part of a three-party consortium that (had) purchased 75 per cent shares of … (Pakistan Steel)" (Iqbal, 2006a: 1).

4. CONCLUSIONS

The analysis conducted in the previous chapter regarding the effects of privatization in the specific context of public sector manufacturing industries in Pakistan clearly distills a primary conclusion – the privatization of public sector manufacturing industries has not proven to be a viable economic policy option in its current manifestation. Neither has the programme delivered its universally coveted efficiency gains, nor has it produced the desired macro-economic results. In fact, privatization of the public sector manufacturing industry in Pakistan has played a part in further accentuating social ills such as wealth concentration, corruption and unemployment. This is especially true for the results following the first wave of privatization in the 1990s, while the impact of latest privatizations is too early and insignificant to judge (especially for macro-level changes) given the small number of transactions that have taken place.

Advantages of ownership, incentives, monitoring, accountability and reduced political interference have produced, at best, modest improvement in efficiency and efficiency related gains. On the flipside, however, incentives have stooped to the level of selling off assets and making money, citizen accountability has seen its new low, ownership change has often implied closure, and corruption has found a new face. The analysis also dispels popular notions of inefficiency, protectionism, and non-existence of competition in public sector manufacturing industries by showing that much of the sector, before privatization began in 1991, was performing reasonably well under a competitive framework, in a less protectionist environment compared to private industries, and with few if any subsidies. In fact the only public manufacturing industry currently granted a subsidy happens to be the fertilizer industry.

The macro-economic results of privatization have also been sobering with little if any positive influence observed on economic growth. Similarly impact on debt reduction has also been minimal. Some fiscal improvements resulting from privatization receipts have been observed but the sustainability of these is questionable given that the corresponding reduction in state expenses/liabilities has often been contingent to the level of benefits and financial cleanup agreed upon by the government. Furthermore, the tax revenue

lost to the government following closure of profitable units after privatization also diminishes the overall positive, if any, effects. On the other hand social problems that have been accentuated in part by privatization – such as increased distributional gap of wealth and assets, decreased real earnings, unemployment, and feminization of labour – continue to hamper Pakistan's progress towards achieving true socio-economic development. Disadvantages of foreign ownership and strategic concerns are potential areas of problems that privatization of public sector manufacturing industries is posing for the economy and the country (no manufacturing unit has actually been sold to foreign owners as yet). No doubt FDI does come in through foreign ownership; however corresponding outflow of capital, which is on the increase in Pakistan, has dampened the overall advantages that FDI brings with it. The near sell-off of the strategic Pakistan Steel and the immediate price hike following its privatization announcement has also raised serious concerns about the fate of dependent industries in the construction and manufacturing sectors. Furthermore, issues of sovereignty are high on the agenda, given that the market has no "patriotic" associations, and once a strategic unit is privatized, it can land into the hands of owners from hostile nations as well.

To make matters worse, the nature of the overall privatization programme is not only imposed but also flawed in several ways. With a rationale dictated by the IMF, a technique accentuating wealth concentration in the society and a process marred by corruption and inconsistency – it is no surprise that the economic and social outcomes of manufacturing industry privatization have been more damaging than constructive. The ensuing objectives that PC aims to achieve through such a flawed process are therefore, at best, ambitious. In fact, as Kemal (2000) points out, privatization is neither a sufficient nor a necessary condition for the fulfillment of some of these objectives. For instance, ownership as shown earlier, is not a necessary criterion for improvement in the quality and quantity of goods and services, because it is the internal cultural environment and management techniques of a firm alongside the nature of external competitive environment that ultimately result in efficiency and its associated gains (Martin, 1993; Cook *et al*, 1988). Moreover, reducing opportunities for corruption essentially requires system reengineering at every level and not programmes for dissociation from the system *per se.* This is because corrupt practices tend to permeate such programmes and open-up newer avenues for corruption (Cook, 1997), which render the achievement of this objective largely futile.

On the other hand, the politico-economic parameters determining the outcomes of privatization have also served to further limit the advantages of this policy instrument in Pakistan. These include amongst others the pre-privatization skewed status of wealth and income distribution (see Hussain, 1999 cited in Srinivasan, 2003), the problematic situation of unemployment (see Aslam 1999) and firmly rooted corruption in the fabric of the society (see TI, 2003). Stated differently, in a fractured society where elite capture, income inequalities, unemployment and corruption in various forms and manifestations are deeply rooted, privatization of public sector manufacturing industries is serving as a cause of further exacerbation of these problems.

All in all, the economic and social disadvantages that have followed the implementation of privatization in the public sector manufacturing industry - both at the firm and the society level - overshadow the advantages that this policy tool has brought about. Moreover, the micro analysis essentially echo's Perevalov *et al's* (2000) conclusion that a change in ownership by itself "on average …(has not) produce(d) performance improvements…" in Pakistan's public sector manufacturing industries (p.351), while the macro analysis reaffirms Cook *et al's* (1988) conclusion that "the size of the public sector (manufacturing industry) *per se* …(has) not …(had) a significant bearing on the performance of the sector or economy" of Pakistan (p.10).

4.1 Is Privatization a Viable Policy Option for the Future?

Having placed the micro and macro economic results of public sector manufacturing industry privatization within the larger context, another very important

conclusion surfaces; privatization *per se* is not an inherently flawed tool, but it is the context of Pakistan, the public sector manufacturing industry and the implementation rationale, technique and processes that have shaped the outcomes ensuing from it. The conclusions also do not go to say that privatization has not had or can never have any positive impacts in the Pakistani context. Examples of public sector units that have shown exemplary performance improvements following privatization, such as Millat Tractors, Bolan Casting, Ravi Engineering, Al-Ghazi Tractors, Balochistan Wheels and Indus Steel Pipe (Siddiqui, 2006a) stand to validate that some improvements have been achieved. Furthermore, privatization has the potential to provide for the much needed capital injection that large-scale manufacturing units require to progressively fulfill their commercial objectives, and which the GoP finds fiscally burdensome to accommodate.

However, turning a blind eye to the limits of privatization can be a dangerous undertaking. Surely, privatization "may be the best option in some cases; but reforming the public sector, may be the better choice in other cases" (Weizsäcker, Young, Finger & Beisheim, 2005: 360). In a nutshell, then, the challenge for the Pakistani state is not to divorce privatization from the wider set of economic policies, but to tailor the nature and form of privatization programmes to suit the politico-economic setup of the country in a way that minimizes economic and social losses. Simultaneously, the government needs to bear in mind alternative policy options and approaches to privatization that may assist in mitigating the problems of strategic public sector manufacturing industries as well as those assigned a distributive function, without having to necessitate change in ownership. In this regard, future policies must focus on building the capacities of the state so that it may play a cardinal role in influencing the maximization of societal gains in conjunction with both the private sector and the civil society.

4.2 Bridging the Public/Private Divide

As concluded in the theoretical chapter, the public/private divide is neither a valid notion nor a healthy approach towards development in the current era of globalization. The idea of governance however, which encompasses the "traditions and institutions by which authority in a country is exercised for the common good" (Kauffman, 2005: 1) calls for instituting the right mix of the public, the private and the civil society, in such a way that the social and economic fabric of the country is strengthened and the institutional structures for development are diversified and fostered.

Given these modalities, the role of the state becomes essentially two-pronged whereby it must not only act as a development agent, but also as a catalyst for synergizing the abilities of the private sector and civil society, because national planning and administration is predominantly the domain of the state (Rojas, 2005e). This scenario assimilated in the context of Pakistan does not paint a radically new picture, because historically the state has been simultaneously involved in broadening and deepening the public sector, and strengthening and guiding the private sector through support institutions. Consequently, the revival of state institutions such as PIDC is imperative. Such an initiative will also allow the state to remain equipped with the necessary expertise to plan and initiate socially and economically desirable industrial projects when they are required. For instance, the government has already planned to initiate two projects under PIDC in order to stimulate industrial and business activities in the city of Karachi. These projects also aim at creating greater employment opportunities by being essentially labour-intensive units (Ghausi, 2004).

Public-private partnerships, which are medium to long term relationships between the public sector, private sector and civil society, and involve the sharing and transferring of risks and rewards (Sampath, 2006), also provide an excellent platform for bringing the development agents of Pakistan together. In the context of manufacturing industries, such a partnership can exist in the form of a joint venture between an established firm and the public sector enterprise (Siddiqui, 2005a). A joint venture refers to "any agreement or arrangement which enables two or more parties to jointly execute some commercial enterprise. The essence of such an agreement or

arrangement is the feature that the business undertaking is a multi-party effort which may take the form of a consortium, a partnership or a joint venture corporation, in which the stakes of success or loss are jointly held by the joint venturers" (Fong, 1985: 4). In this context, institutions such as universities or R&D units can also be partnered for technology development, technology transfer or technology assistance (NSF, 2006). Non-profit organizations can also be included in the partnership for their expertise in providing training services to workers and staff and assisting in upgrading their knowledge, adaptability and consequently market value.

4.3 Salvaging the Remaining Public Sector Manufacturing Industries

Although today, much of the public sector manufacturing industries have been privatized or shut-down, all is not lost and policies can still be altered to salvage what is left (Table-4.1). This is especially true for the heavy engineering units still functional under SEC, because some of these units are one-of-a-kind facilities in Pakistan (Siddiqui, 2005a; 2006a; 2006b; 2006c) which require dedicated and planned capital injection as well as necessary avenues for tapping into export markets in order to realize maximum capacity utilization and economies of scale (Auty, 1994). Much investment has already been made in these capital intensive units and Pakistan should be looking at ways of reaping long-term economic benefits out of these rather than selling them off for an amount that might not even be reflective of the opportunity cost of investment tied up in these projects for years. These units were built with the mission to promote indigenization and self-reliance in production (SEC, 2004) and possess the capacity to influence a reduction in Pakistan's import bill, provided they are given a chance.

HMC is a prime example of the domestic and export commercial potential of a unit that was established to spearhead indigenization in engineering industry rather than attain profit maximization. Yet, the unit has helped save billions of dollars worth of imports to the government while simultaneously earning billions more through exports. Although the 1990s were a bad patch in the accomplishments of the unit, it has managed to find its rhythm again, but is on the active list of privatization planned for this year (Siddiqui, 2006a).

Salvaging SOEs is not a new phenomenon even in the globalized world of today. France is a good example of how the state has remained committed to the policy of creating "national champions out of strong domestic companies, and … (ensuring)… that weak companies stay(ed) alive and French" even in the competitive international arena (Economist, 2004: 2). In 2004, the French government bailed out Alstom – "a troubled French conglomerate that makes trains, turbines and ships" – whose turbine division was being eyed for a take-over by the German engineering group, Siemens (Economist, op. cit. p.1).

The following discussion brings together a few broad options that can be exercised to complement or substitute future privatization of manufacturing units within the political economy constraints of Pakistan.