

Budgetary Impact of State-owned Enterprises

The writer has contributed this article exclusively for the current issue of CMA Journal

The Aggregate Annual Report on Federal State-Owned Enterprises (SOEs) has recently been released for 2022-23 by the Central Monitoring Unit (CMU) in the Finance Division, Government of Pakistan. This is a very useful report and quantifies the key financial indicators at the overall, sectoral and individual SOE level.

There is need first to get an estimate of the size of the role of SOEs in the national economy. Altogether, there are 88 commercial SOEs. The total value of sales of these SOEs in 2022-23 was Rs 11.922 trillion, with an annual growth rate of 15%. A comparison can be made with sales by all public limited companies in Pakistan. This is estimated at close to Rs 21.0 trillion in 2023. As such, the SOEs collectively also play a significant role in the economy.

Another significant indicator is the collective contribution of SOEs to the federal revenues. This is estimated at Rs 466 billion in tax revenues and Rs 952 billion in non-tax revenues. However, the latter magnitude probably also includes the SBP profit of Rs 371 billion transferred to the Government of Pakistan in 2022-23.

As opposed to this, the CMU report says that the aggregate budgetary support provided to SOEs was Rs 1021 billion in 2022-23. This consisted of Rs 403 billion of subsidies, Rs 223 billion of grants, Rs 128 billion of loans and Rs 267 billion of equity injections.

The total book value of the assets of the SOEs was Rs 35.2 trillion in 2022-23, while

the liabilities were Rs 29.7 trillion. The net equity is Rs 5.5 trillion. Overall, there was a net loss of Rs 202 billion. SOEs in two sectors have a high level of profitability. These are the oil and gas and the banking sectors. The biggest losses are in the power, infrastructure and transport sectors.

The four biggest profit-making entities are the Oil and Gas Development company (OGDC), Pakistan Petroleum Ltd. (PPL), the Pak-Arab Refinery and the National Bank of Pakistan (NBP). The four biggest loss-making entities are the National High Authority (NHA), the electricity DISCOs, PIA and the Pakistan Railway.

The power sector is the most problematic sector. The circular debt was over Rs 4 trillion and bulk of the subsidy from the Federal budget to SOEs goes to this sector. Despite this support, power and gas tariffs have escalated rapidly. This has caused significant cost-push inflation as well as badly affected the competitiveness of Pakistan's exports.

There has been much discussion on large-scale privatization of SOEs to reduce the existing burden on the exchequer. It is estimated that the magnitude of this burden on the Federal budget will be as much as Rs 1850 billion in 2024-25. This is equivalent to an increase of 68% over the level in 2022-23, estimated by the CMU. The largest share in this burden of 67% will be in the form of subsidies, especially to the power sector, followed by 25% as grants and 8% as loans or equity injections.



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There have been different rounds of privatization in Pakistan's history. A total of 169 units have been privatized since 1991. This includes 31 banks and financial companies, 14 energy units, 105 industrial units, 4 in the telecom sector and 15 in other sectors. Both profitable and loss-making units have been privatized. It is interesting that as far back as 2014, privatization of PIA was included in the on-going IMF Program.

There is need for a proper technical and objective analysis of the case for privatization of a particular SOE. It is essential that explicit criteria be identified and applied to evaluate the case for privatization of a SOE.

An attempt is made to identify some of these criteria. The first relates to the level of profitability. If the SOE is loss-making then this strengthens the case for privatization.

Second, the issue is whether the SOE is operating in a competitive market or is effectively a monopoly. Privatization would risk the increase the exercise of monopoly power by a private owner. This is illustrated, for example, in the case of behaviour by K-Electric, the only privatized DISCO currently. It has engaged in discrimination among consumers and limited the supply of electricity to low-income neighborhoods in the city of Karachi.

Third, it is essential there be already a proper valuation of assets and liabilities of the SOE under consideration for privatization. This is clearly a problem with PIA, with large outstanding liabilities and the extent to which these can or will be transferred to a new owner.

Fourth, the privatization case becomes weak if the SOE is performing social functions. Fifth, if there is evidence of substantial over-employment which has badly affected profitability, then this strengthens the case for privatization.

The above five criteria have been applied on the basis of the CMU data on individual SOEs. There is a case for privatization of PIA and PNSC in the transport sector, but clearly not of the Pakistan Railway. It also turns out that the case for privatization of the power sector DISCOs is not very strong on the basis of the above criteria.

The Federal budget of 2024-25 indicates that it is unlikely that there will be significant process of privatization this year. Only Rs 30 billion of privatization proceeds have been budgeted for. It remains to be seen how large and comprehensive a privatization program will be agreed with the IMF in the impending new three-year Extended Fund Facility.

Overall, one of the key areas of reform in the forthcoming three-year IMF Program will be on achieving a big reduction in the burden imposed by the SOEs on the Federal exchequer and on the national economy. The first indicator of progress will be the privatization of PIA. The next area of focus will have to be on strong management improvements in the power sector and reduction in the extremely high level of distribution and billing losses.

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