



## Industries and Privatization

### Towards Industrial Recovery

As a result of international recession, energy shortages, and a contraction in the economy, the industrial sector in Pakistan has been adversely affected. This sector posted a negative 3.3% growth in the outgoing year with large-scale manufacturing posting a negative 7.7% growth. The industrial sector is our engine of production and employment, but it is fragmented and lacks consolidation. The Government has proposed to declare 2009-2010 as the Year of Industrial Recovery, and it providing the following support measures to this sector:

### Financial Measures:

With a view to moving industry towards consolidation and value addition, an Export Investment Support Fund, worth Rs.40 billion has been proposed for 2009-2010. The Government will contribute Rs.10 billion towards this fund; another Rs.10 billion would be contributed by the Export Development Fund; balance Rs.20 billion would be contributed by Government agencies through mopping up of surpluses in commercial banks.

In order to support the small and medium enterprises (SME) sector by providing access to credit, a fund worth Rs.10 billion for Credit Guarantees is going to be established. This fund would be financed by the Government and the private sector in the ratio of 50:50 over the next two years. The Government has already proposed Rs.2.5 billion in the Budget 2009-2010 as its share to the fund.

For citizens who lack equity financing, a Venture Capital Fund of Rs.10 billion is also proposed to be established, which shall be financed in the same manner as the SME Credit Guarantee Fund. A provision of Rs.2.5

billion has again been proposed for this fund in Budget 2009-2010.

A new DFI is being created for industrial financing.

Industrial clusters are going to be involved for the skill development to ensure ownership, monitoring/oversight and relevance of programs.

The allocation for Ministry of Industries has been increased by 335% from Rs.2.0 billion in 2008-2009 to Rs.8.7 billion in 2009-2010.

The budgetary allocation for Science and Technology has doubled from Rs.1,510 million in 2008-2009 to Rs.3,140.4 million during 2009-2010.

Government is not going to enhance tax incidence on industry, except tobacco; rather following tax facilitations have been proposed:

In order to assist automobile manufacturers and their vendor industries, a reduction of 5% excise duty on automobiles is proposed;

In order to revive the construction sector, a reduction of Rs.200 per ton in the excise duty on cement. This decrease shall be passed on to the consumer.

In order to support the textile sector, withdrawal of federal excise duty on import and supply of Viscose Staple Fiber and zero rating of chemicals used in manufacturing of fire retardant fabrics is proposed.

Cellular service providers have been provided the following relief:

- Elimination of Regulatory Duty of Rs.250 per set.

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- Reduction in Customs Duty from Rs.500 per set to Rs.250 per set.
- Reduction in Excise Duty from 21% to 19%.
- Sim activation charges reduced from Rs.500 to Rs.250.
- Incentives for documented sector in case of 90% purchases from sales tax registered suppliers.
- Zero rating duty on exports sector will continue this year as well.
- To protect the local industry from under invoicing by importers, improvement in Customs valuation and enforcement mechanism would be ensured.
- Refund procedure would be streamlined – Federal Board of Revenue to pay interest on refunds delayed beyond 90 days.

billion in 2007-2008 and dropped further to \$9.6 billion in 2008-2009 due to global recession and some domestic impediments. However, the textile exports during July-January 2009-2010 increased by 2.27% as exports during the period were recorded at \$5.945 billion against \$5.814 billion recorded during July-January 2008-09.

Realizing the importance of the sector for economic growth and the impending challenges, the Government, in August 2009, embarked upon an ambitious plan and launched the first-ever Textile Policy 2009-2014 with an aim to achieve the objectives of economic growth and poverty alleviation. The textile policy envisages achieving an ambitious export target of \$25 billion till 2014 through universal development of the textile value chain and focus on development and up-gradation of skills, technology and infrastructure to create an environment for growth and job creation.

The Textile Policy gives a roadmap for employment generation, value addition and efficient use of domestic resources to maximize the gains from the potential available. Since the Government firmly believes in encouraging private entrepreneurial initiatives, therefore, the policy firmly enshrines the objective of development through public-private partnership. While the Government has committed to provide support, it would essentially act as a catalyst to spur private sector initiative including investment, research and up-gradation.

In order to implement the major initiatives of the Policy, the Government has already issued notifications including:

1. Draw-back of Local Taxes and Levies Order 2009
2. Export Finance Mark-up Rate Facility Order 2009
3. Mark-up Rate Support for Textile

### Competitive Textiles

The textile sector is the most important export sector of the country, which contributes around 54% of the export earnings; employees 38% of the industrial labor forces; besides generating 8% of GDP. More than 80% of the country's textile production is exported and the rest is consumed domestically. There has been negative growth in textile exports since 2007 due to global slow-down and certain domestic factors. However, owing to initiatives taken by the People's Government, the textile exports witnessed positive growth during 2009-2010.

Data shows that textile exports in 2006-2007 were \$11.3 billion, which dropped to \$10.7

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4. Re-imbursalment of Employees Oldage Benefits Institution Contribution Order 2009 was issued on September 30, 2009.
5. To refund the past claims of R&D Support scheme as announced in the Textile Policy, State Bank of Pakistan has been directed accordingly.
6. Directions have also been issued to the SBP to continue the monetization of customs duty at PTA @ 7.5% during 2009-2010.
7. In order to zero-rate the import of Textile Machinery as announced in Textile Policy 2009-2014, FBR has issued SRO No.809(I)/2009 dated 19.09.2009.

The Textile Policy has made special focus on diversifying the product base and encourages use of fibers other than cotton. The Government would also ensure skill development and research through synthetic fiber development and application center to facilitate the manufacturing of finer filaments for value addition. A ginning institute will be established at Multan to undertake research in improved ginning methods and provide training for improved efficiencies, while steps would be taken to identify clusters for the traditional textiles (handloom, embroidery, handicrafts and carpets).

The Ministry of Textile Industry is also establishing Pakistan Textile City in Karachi to promote textile sector. The initial share of the Federal Government in the paid-up capital of textile city was Rs.500 million while during 2008-2009, credit line of Rs.500 million was established by National Bank of Pakistan through Government guarantees. In addition, the Government has committed to provide a guarantee of Rs.1 billion for the project.

Three garment cities are being established in

Karachi, Lahore and Faisalabad. The Government would take measures to promote manufacturing of indigenous machinery and chemicals and other support industries.

The textile sector has grown to be the single largest manufacturing sector of Pakistan. However, support industries -- like textile machinery manufacturing, textile dyes and chemicals, and accessories industry -- have not developed commensurately, and that is why most of the demand is met through imports.

Yet another milestone was achieved when Korea International Cooperation Agency (KOICA) agreed to provide assistance for the establishment to Garment Technology Training Centre (GTTC) in Karachi and agreed to provide an assistance of \$1.5 million, while some expenses of the project would be borne by the Federal Government through PSDP.

In pursuance of implementing the Textile Policy, the Textile Ministry has already taken initiatives and issued several notifications in this regard. It intends to promote and encourage the textile industry to boom and flourish for enhancing exports to help ensure sustainable economic growth. The effects would ultimately trickle down to the common man and the poor, thereby helping to alleviate poverty and help ensure standard living for all.

### Privatization: A New Vision

Privatization was initiated in Pakistan by Shaheed Mohtarma Benazir Bhutto's first government in 1988 as an economic reform policy tool in order to improve the efficiency of economic concerns run by the Government, since most of the public sector entities were under-performing and were not

fully utilizing the available resources of manpower and fixed assets. However, during the last authoritarian regime, it developed into an avenue for reducing budget deficit without any consideration to improve efficiency of the entities or to enhance Government revenue on a sustainable basis.

The People's Government took a pause from mindless privatization and reviewed the whole policy spectrum in a meeting presided by the President of Pakistan on December 31, 2008. President Asif Ali Zardari observed that most of the public sector entities were under performing and were not fully utilizing the available resources of manpower and fixed assets. He stressed the need to co-opt private sector, adopt new framework and develop such transaction structures where the back-end profits and benefits to the Government in terms of management and financial position of state-owned enterprises (SOEs) will have a greater upside versus up-front payment of one-time sale consideration. This will provide the Government an upside on its ownership and maximize the value of its equity.

The President directed that existing privatization policy of strategic sale (51%-100% shares) should be reviewed and be modeled around the concept of public-private partnership (PPP). The concept envisages that the management may be transferred to investors through sale of 26% shares while ensuring transparency and all other aspects safeguarded through comprehensive documentation. This strategy is based on the rationale that given the large size, a single offer for total divestment for some transactions would limit the interest of potential investors and consequently affect the level of competition. It also helps to sell the remaining equity in a phased manner so as to maximize the eventual sale proceeds once the private sector has had a chance to bring about substantial value addition to the SOE.

The main objective of privatization of 26% equity stake with management rights through a PPP model is to put national resources and assets to optimal use and, in particular, to unleash the productive potential inherent in Pakistan's SOEs. The Government would continue to ensure that divestment does not result in alienation of national assets and reduction in quality of production and service to the detriment of its people. It would also ensure that divestment does not result in private monopolies and cartels.

A sound contractual regime working under the enabling provisions of law would be put in place to accomplish cutting-edge innovative PPP structures reflecting best international industry practices, particularly for utilities, tourism, retail, infrastructure, and services sectors.

Prior to the inception of the PPP mode of privatization, the proceeds had been used for budgetary support; but now the prime target is to increase competitiveness, improve efficiencies, to bring in latest technologies with the technical people to run the entities in a thoroughly professional manner, which would also provide the Government an upside on its ownership and maximize the value of the entity. It will also ensure back-end profits and benefits to the Government in terms of Management and Financial positions of SOEs with a greater upside versus up-front payment of one-time sale consideration. The Government interest would be protected through appropriate representation on the Board of Directors of the privatized entities. The working of privatized assets will be monitored by the Board of the Privatization Commission.

Workers are important stakeholders of public sector enterprises and the Government will take them on board at every step by creating a sense of ownership among them. The Government has restored the services of unlawfully terminated employees of the

public sector enterprises with their due benefits. The President has declared them co-workers and partners in ownership along with the Government and the private sector.<sup>1</sup>

The new Privatization Policy has been carefully designed to ensure the continuation of services of the existing employees whereby the Government will retain majority shares and the private sector partner will invest in expansion of the business, thus requiring more employees. According to the new policy, the employees will also be offered 12% shares of the public sector entities,

whether privatized or not.

The new policy will benefit the people in a number of ways. It will enhance competitiveness of the entities thereby reducing the prices. It will also engender growth in the economy, thus reducing poverty. It will create broad-base ownership, which will ensure that the fruits of development are shared by larger number of people.

## Industrial and Trade Development in Pakistan

By Zubair Faisal Abbasi

The last two years have been witness to a decline in the industrial and trade development fortunes in Pakistan with wide-ranging implication for economic growth. During 2008-2009, large-scale manufacturing witnessed negative growth of 7% while value of imports increased to almost double of the export. The phenomena, however, has a history of policy orientation behind it. In fact, as predicted by a number of international researchers, the rapid liberalization of trade regimes along with dismantling of industrial policy during the late 1990s and 2000s, there has been progressive increase in trade gap and unsatisfactory performance in industrial competitiveness and development.

Historically speaking, many researchers argue that Pakistan was unable to craft and implement a planned scheme of industrial development and up-gradation leaving continued absence of a national system of innovation. It failed to facilitate and execute inter-sectoral linkages amongst trade, industry, banking, and education sectors, which could design the required social infrastructure for sustained economic development. On another account, unlike many late industrializers of East Asia, the role of the State in Pakistan remained questionable in allocation of resources for rapid industrialization and modernization of economy. As mentioned by Dr. Asad Sayeed, the regulatory and financial systems served on the basis of political alignments with the regime instead of creating a genuine entrepreneurial class.

However, after wasting the 1980s despite having massive 'big push' by the public sector from the 1970s, the 1990s were strangulated under structural adjustment programs. It must be noted that during 1990s, there have been frequent settling and unsettling of political regimes with interim governments playing a big role in the management of economy. During this time, a serious effort for implementation of the Washington Consensus approaches wedded to the policies of

'liberalization, stabilization, and privatization'. It focused more on what is called 3D approach, i.e., Dismantle the State, Dis-empower the worker, and Depend on the market. The trend continued and the economic management of Pakistan took a slow but sure turn from being predominantly developmental to neo-liberal idea system.

But despite having a structurally adjusted economy, the fortunes of industrial sector have not flourished. The economic management acumen could not bring the required social infrastructure, which is essential for pro-poor growth in industrial and commercial capital. There is no exaggeration that it is the industrial and manufacturing sector, which helps create valuable items for exports as well as generates employment and labor utilization potential in an economy. Empirical evidence from many countries, including from East Asia and China, shows that poverty can rapidly and substantially be reduced only in those economies, which can create a flourishing industrial sector and modernize the agriculture segment.

If we look at Pakistan, during the period between 1999-2000 to 2007-2008, the growth rate of the banking and finance sectors was much higher than the industrial and agriculture sectors. The commodity and electricity shortages that were witnessed later in 2007-2009, are not a product of one or two years. There were acts of omission and commission, which failed the State to enable itself in playing a more constructive role in trade and industrial development of Pakistan.

The current economic management needs a politically embedded role of the State to create vision for economic management and follow up the vision with developing appropriate institutional arrangements. Despite having vast resources for material progress, Pakistan was not able to create a turnaround and catch up with the industrial world, let alone make a strategy to forge ahead. In one sentence, democratic Pakistan needs to seriously revisit the trade and industrial development vision, if it wishes to develop a high-quality pro-poor economic development that reduces the incidence of poverty.

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<sup>1</sup>Dawn, March 6, 2010.