

Privatisation of SOEs: a focus on PIA

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Pakistan's economy is confronting numerous challenges like fiscal deficits, low savings, limited investment, low foreign exchange reserves, economic uncertainty, and rising external debt, expected to reach about \$131.159 billion at the end of the first half of the fiscal year 2024 (July-Dec).

Furthermore, state-owned enterprises (SOEs) substantially burden the already struggling economy. They are loss-making entities that have repeatedly received government bailouts, resulting in colossal losses for the national exchequer. As of December 2023, these enterprises' total outstanding debt and liabilities stand at PKR 2.35 trillion. To achieve fiscal discipline and stabilize the economy, the government chose to privatize the unprofitable state-owned enterprises (SOEs), with Pakistan International Airlines (PIA) as the top priority.

Pakistan International Airlines Company Ltd (PIACL) was established on January 10, 1955, through a merger with Orient Airways, founded in 1946. The national flag carrier gained global prominence as it expanded its fleet and developed extensive air routes under the leadership of visionaries like Air Marshal Nur Khan and Air Marshal Muhammad Asghar Khan.

Despite its early success, PIA gradually deteriorated and began facing financial challenges starting in 2008.

The company's balance sheet showed a negative equity of PKR 490 billion (as of June 2022), which included bank loans and other payables. As of June 2022, total outstanding bank loans and government guarantees are PKR 109 billion and PKR 268 billion, respectively.

The deterioration of the airline can be attributed to several factors, including increased political interference and a highly politicized and poorly trained workforce. The airline also struggles with an outdated fleet and high operational expenses to maintain it, particularly on financially unsustainable routes. Additionally, non-core functions such as ground services, catering, and courier services have added to the company's burdens. PIA faces tough competition due to the 'Open Sky Policy,' which has led to a decline in its market share. Frequent management changes, undue influence exerted by unions and associations, political interventions, wasteful spending, unchecked borrowing, and a lack of internal accountability mechanisms have further contributed to the decline of the national flag carrier.

Other challenges included a fake pilot license case, poor airport infrastructure, operational

inefficiencies, flight delays, and massive corruption by the Cargo department. Union protests, increased fuel prices, and an EU-imposed safety ban on PIA's flights to Europe in 2007 exacerbated the situation, leading to total financial losses of up to 724 billion by the end of 2023.

The Government of Pakistan (GOP) intends to partially privatize PIA by selling 51% of its share and management rights to overcome these financial and governance issues. This restructuring will separate aviation-related components from non-core elements, thus relieving functional units from some debt.

For this purpose, a PIA holding company is established to manage airline debt, including Rs. 243 billion by domestic commercial banks, a foreign loan of \$88 million, and to facilitate privatization by assisting with transfers.

The first inaugural meeting of a board consisting of 7 board members headed by Tariq Bajwa (former central bank Governor) on March 27, 2024, endorsed a scheme of arrangement approved by both stakeholders and creditors.

The airline's sell-off is expected to bring \$250-300 million to the government; however, the actual value can differ. According to the Federal Minister for Privatization and Investment Board Abdul Aleem Khan, the Privatization Commission has received expressions of interest and statements of qualification from 8 major business groups, signaling a strong interest in the future of PIA.

The privatization initiative is anticipated to lead to a positive transformation. It is expected to enhance efficiency and productivity, attract private investment, and improve competitiveness and service quality while safeguarding public interests.

However, it is crucial to regulate the process to prevent potential negative outcomes such as increased unemployment, limited access to flight routes in marginalized regions, and monopolistic practices.

To fully capitalize on the advantages of privatization, we can draw on the successful experiences of other nations as a detailed guide for making well-informed decisions. For instance, Sri Lanka, the United Kingdom, Latin America, France, and Germany have turned their loss-making SOEs into profitable entities.

The privatization of Sri Lanka Telecom in 1997 and Sri Lankan Airlines in 1998 transformed them into highly efficient and profitable businesses.

Similarly, the privatization experiences of British Airways, Lufthansa, and Air France vividly illustrate the resounding success of airline privatization in Europe. British Airways underwent privatization in 1987, and the subsequent organizational restructuring propelled it to become one of the leading airlines today.

Lufthansa, the flag carrier of Germany, was privatized in 1994 and currently ranks as the fourth-

largest airline in terms of revenue.

All these nations have followed almost a similar privatization process, including intra-firm planning by streamlining procedures and strategic approaches, as well as broader changes like alliances and mergers.

Along with the deregulations, the scale strategy aided in establishing relationships with airlines through investments and code-sharing agreements, consolidating market power and global network.

The 3Cs framework - Competition, Cooperation, and Consolidation - summarizes the reason behind the successful privatization of these entities.

The successful privatization of these organizations can provide valuable guidance for Pakistan's effective privatization of PIA and other SOEs. It is essential to establish a stable macroeconomic framework that prioritizes developing institutional capacity with the support of strong regulatory bodies. These entities can oversee the restructuring phase during the post-privatization period, ensuring transparency and integrity.

Clear, comprehensive, and coordinated approaches that consider all parties' interests and prioritize transparency, inclusivity, and affordability for consumers can help achieve favorable outcomes of privatization. This includes reducing the fiscal burden and paving the way for sustainable development, all while safeguarding public interests.

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