

## Privatization and Reasons for Government's Failure to Implement It

Akhbare Eqtesad [Economic News] (Morning Daily)

Saturday, Feb. 19, 2000, No. 132

By: Ebrahim Emad (Ph.D in Law of International Economy & Development)



### Summary:

Privatization was one of the main pivots of the programmed adjustment structure (PAS) implemented in Iran from 1989 to 1994.

Various views have been expressed on ways of implementing this policy and reducing the government's control of economy.

In the following article, Ebrahim Emad, an international economic and legal expert, while referring to the experiences of privatization in Iran has offered some proposals to insure the success of the privatization policy.

### Text:

Privatizing the state-owned companies as one of the processes of the programmed adjustment structure (PAS) was a plan raised by the International Monetary Fund (IMF) in 1987 at the international level and the then government of the Islamic Republic of Iran decided to implement the plan within its First Five Year Development Plan.

In April 1991, the then Cabinet ministers, based on the authority given to them by the Articles 34 and 138 of the Constitution and policies of the first part (1) of the First Five Year Development Plan approved in 1989, endorsed the policy to cede shares of state-owned companies and organizations to the private sector with an aim of boosting economic activities, easing the government's involvement in such activities or in unnecessary services, except for parent industries, enforcing the economic adjustment plan and making optimal use of the country's facilities. Two lists of companies subject to this decision were prepared with the first list containing 248 state-owned companies and the second 143 (2).

As for the companies included in the first list, the representatives of the government to the general assemblies of those companies were assigned to carry out all formalities concerning the ceding of their shares.

As for the companies contained in the second list, a commission comprising the ministers of economy and financial affairs, of industries, of heavy industries, and of labor and social affairs as well as the head of the Plan and Budget Organization and governor of the Central Bank of Iran had to be formed under the chairmanship of the first vice president to study and make decision on the transfer of those companies after getting the approval of the cabinet ministers.

Under this approval and in order to help the workers and other employees working in those manufacturing units, transfer of 33 percent of the shares at the current prices to them has been predicted and they have been given one year from the date of share offering to announce their decision.

In the course of 1991, the cabinet approved a plan to privatize some other state-owned companies particularly the auto manufacturing plants which had been introduced by the Ministry of Heavy Industries.

In March 1992, the government decided that the share of state-owned companies be ceded through three methods of sale at :

- 1. the Tehran Stock Exchange,**
- 2. public tender**
- 3. direct sale to applicants.**

In the same year, new companies were proposed for privatization by the Ministry of Health, Mines and Metals Ministry and Kish Development Organization. In some cases, the ceding of shares could be carried out in the form of transfer from a ministry to another state-owned or state-run company.

In December 1992, all affairs relevant to policy making, programming and adoption of other necessary measures for transfer of the shares belonging to the government and state-owned companies were entrusted to the Economy Council in order to expedite the trend of privatization. Under policies adopted by the Economy Council, a secretariat was formed under the supervision of the Ministry of Finance and Economic Affairs to make necessary planning bring about coordination among the organs offering their shares and supervise the way the shares were transferred.

In 1993, the government approved a plan to transfer the industrial and commercial representation of the Tobacco Company to the private sector.

In November of the same year, the then minister of finance and economic affairs speaking at a seminar on privatization held at the Bank Sepah's club (3) in Tehran summarized the long term goals of the privatization program as follows:

- To enhance the efficiency of manufacturing units as the most important goal of privatization,
- To reduce pressure on the government budget,
- To gain access to international capital and technology markets and renovate the technologies existing in the country,
- To attract people's capitals and involve people in the national production,
- To provide job opportunities in the long run,
- To pay attention to the fact that the wealth and natural resources belong to all Iranian generations and therefore it is not fair to use these resources for one generation alone.

From March 1994 onwards the trend of privatization began to decline and the issue was rarely raised by the mass media or in the cabinet meeting. However, besides the aforesaid lists, a few other companies have been introduced for privatization. **There has not been a complete**

list of companies owned or run by the government nor has the public welcomed as enthusiastically they should the shares offered by those companies through the Tehran Stock Exchange.

Given the fact that the process of privatization should be carried out in concert with other factors of the **Programmed Adjustment Structure** as desired by the **International Monetary Fund** such as determining the real value of the national currency against foreign exchanges, reducing the liquidity, reducing the budget deficits, decreasing and stabilizing wages level, facilitating free foreign trade, easing the government's role in the economy, reducing government expenditures, implementing free market economy, providing facilities for inflow of foreign capitals and so on, but in practice there has not been such coordination and harmony.

The scrutiny of the laws, regulations and other decisions approved by the then cabinet ministers from March 1991 to March 1993 forms this question in one's mind that

- why the then government, despite being given necessary authority by the constitution and state laws, **was unsuccessful** in implementing the Programmed Adjustment Structure in the said period?
- Should this failure be blamed on a two year delay between the adoption of the first five year plan law and its approval and the decisions taken in regard to how the shares of state-run companies must be transferred or on giving all decision making authority to a single person for example a minister, or did it stem from personal preferences on the part of top level decision makers such as the then president or ministers and their affiliated managers?

Before giving replies to these questions, reference should be made

- to the high number of state-owned companies including those owned by the government from the beginning and those which due to confiscation and other factors have been transferred to the government later,
- the current budgets of these companies and their upwards trend compared with the total annual budget of the government,
- the growing number of various state-run committees and other establishments along side these companies which in turn have sharply increased the government expenses
- and the efforts of the then **government and the Central Bank** of Iran to keep alive the economic activities of these companies despite knowing that the majority of them were non-profitable, by allocating foreign exchange at the official rate to them in order to meet their expenses, and allowing them in some cases to sell their foreign exchange allocation on the black market at much higher prices, are among other issues that must be discussed,

that because of **the non-profitability of these companies and their unfair access to such facilities, compared with other economic sectors such as cooperatives and the private sector, the Central Bank of Iran faced huge financial obligations.**

**If we take a look at the process of privatization from legal point of view, these obligations are considered among the debts of the state-owned companies and the Central Bank of Iran. These huge commitments discourage purchasers from buying the shares of these companies because from legal point of view, these companies are regarded as those with huge debts and**

non-profitable whose survival depends one **hundred percent on subsidies** and therefore no room will be left in this process for domestic or foreign purchasers.

**As for the obligations of the state-owned companies towards the Central Bank of Iran (CBI)**, we can mention a speech delivered by the CBI Governor Mohsen Nourbakhsh at the 7th conference on monetary and foreign exchange policies (4), on lack of financial balance.

**Nourbakhsh** put the **total debts** of these companies to the Central Bank until March **1997** at **23,216 billion rials** and predicted that the figure would increase by **4,383 billion rials** in **1998**, by **2,753 billion rials** in **1999** and by **977 billion rials** in **2000**.

If we add these figures we will get **31,329 billion rials** as total until March **2000** which is equal to over **412 billion dollars** (at unofficial rate of dollar against rials) and to nearly **18 billion dollars** (at the floating rate of dollars against rials - one dollar = 1,750 rials).

If we assume that all these figures offered by the governor of the Central Bank are correct, then we will realize the position of the state-owned companies in terms of their obligations and debts to the Central Bank. **Considering this situation, will the current government be really able to continue the process of privatization?**

A comparison between the two figures of **412 billion dollars** and **17 billion dollars**, reveals a **2,300 percent reduction in the value of rials against the dollar.**

The points mentioned above indicate only one example of the bad performance of top policy makers including the then president and the Central Bank governor which altogether has minimized to nearly zero the capability of the current government and the Chief Executive in implementing such an important economic process.

**As long as the monetary and foreign exchange policies remain unchanged and as long as Central Bank officials whose policies over the past few years have had no results but high inflation, economic recession and Iran's isolation from world economy remain in their posts, there would be no hope for proper implementation of the privatization policy which the current government has to do at any cost.**

With a close watch of the events one can summarize the **inability of the previous government to implement this process** as follows:

1. The government's growing grip over and involvement in economy and trade particularly foreign trade
2. Adoption of such monetary and foreign exchange policies as multi-parity rates of foreign exchange (official, preferential, competitive, export, and open market rates) and insistence on implementing these policies despite the appearance of their negative impacts on the society and confusion of economic agents, particularly exporters.
3. The lack of commitment on the part of some high ranking government officials to economic and trade operations and combination of these activities with the personal interests of those officials and their political and family affiliates.
4. Non-approval of necessary regulations and lack of sufficient follow-ups since 1994.
5. Existence of uncertainty over implementing the principles of the Programmed Adjustment Structure and lack of coordination between officials of the ministries in charge of implementing these principles.

6. Lack of a balance in granting foreign exchange credits to the three branches subject to the Article 44 of the Constitution, hostility towards the private sector and over exploitation of the state-owned companies despite being aware of their non-profitability. In other words, the Central Bank was tuned into a machine to meet the exorbitant demands of the state-owned companies.
7. And ....

With regards to the aforesaid points the Central Bank insisted on and continued implementation of multi-parity foreign exchange rates and those at the helm of the bank, upon an order from the then president, granted large amount of foreign exchange credits to the state-owned companies from 1992 to 1997 and in the conference on monetary and foreign exchange policies held in Tehran revealed, knowingly or unknowingly, the results of their measures.

As long as these regulations and principles are not improved and as long as officials in charge of these organs particularly the Central Bank are not replaced, there would be no hope for an improvement in the monetary and financial status of the state-owned companies which every year swallow a major part of the government budget without making any profits and whose products, because of high costs of production are not, and will not be able to compete with foreign products on the international markets.

In conclusion, it can be said that privatization can be carried out in the best possible manner only when it is part of a comprehensive reform program offered by a reformist government under a strategic time-table and without allowing anybody to derive personal benefits from it.

**The following points can be mentioned as some advantages of privatization:**

1. Growth of the private sector and creation of a healthy competition in the production sector and people's direct involvement in economic activities and creation of job opportunities
2. Increasing the efficiency of the production sector and curbing inflation
3. Creating an atmosphere of confidence for domestic and foreign businessmen and helping boost the export of non-oil commodities
4. Attracting foreign and domestic investments in the form of hard currency or modern technologies
5. Bringing about further harmony with the international economic system in order to join the member countries of the World Trade Organization
6. Gaining access to modern managerial techniques and getting away from outdated and traditional managerial methods
7. Diluting the government's role in the economy, improving the budgetary structure, reducing budget deficit and cutting government expenditures
8. Improving taxation system and exploring new financial sources for the government to invest in infrastructures
9. Reducing and stabilizing wages and salaries and offering goods at competitive prices

10. Improving social security system and so on

**Footnotes**

1- Official newspaper No. 13134, dated April 1, 1990

2- Official newspaper No. 13491, dated July 7, 1991

3- Ettela'at newspaper No. 20052, dated November 8, 1993

4- A collection of articles presented at the 7th conference on monetary and foreign exchange policies, published by the Banking and Monetary Research Institute 1997, pp 17 - 18

www.ebrahimemad.net