

The forthcoming budget and the public-private mantra

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The government has decided to increase spending in the development sector in the coming year as is evidenced by the expansionary fiscal policy adopted in the forthcoming budget for the year 2009-10. Approval of the highest ever Public Sector Development Program by the National Economic Council comes at a time when many fiscal space constraints are evident—decline in revenues, competing priorities particularly in the wake of the ongoing security situation and efforts to curtail the fiscal deficit in order to keep it within stipulated limits. The rationale for the approach has fueled a debate amongst subject experts—a positive development indeed given the potential within constructive and substantive technical dialogue to shape policy decisions in national interest.

The purpose of this comment is not to dwell on that debate but to draw attention to a related issue of strengthening the public-private interface as a policy option to assist the government in achieving the development objectives envisaged in the budget. Two areas appear important in this regard.

The first area is infrastructure development. In today's environment, investments in infrastructure are critically needed, as they can generate economic activity and create employment. In the 1930's, one of the factors responsible for United States' recovery from the Great Depression related to Roosevelt's policies of investment in huge public work schemes, which enabled the generation of employment. Efficient infrastructure can also boost economic recovery through promotion of local and foreign investment and business productivity and expansion—all of which are needed in today's

context.

The currently prevailing power shortage—though attributable to some extent to the issue of circular debt, the decades-long intransigency to invest in water reservoirs and the crumbling state of public transport and social infrastructure in the country also reiterate the need to invest in infrastructure. Pakistan's overall infrastructure needs have been estimated at US\$500-600 billion. However, as opposed to this, last year's PSDP allocations (2008/09) for infrastructure development approximately stood US\$4-5 billion, and this year's PSDP allocation through increased will also fall short. In view of resource limitations, the government has decided that many infrastructure projects, particularly those related to the transport sector, should be developed and implemented through public-private partnership under the umbrella of the Infrastructure Project Development Facility (IPDF) with support from PPP Infrastructure Cell of the Planning Commission. If appropriately structured, this approach can save Rs. 200-300 billion in PSDP expenditures.

While it is critically important to undertake projects in the PPP mode, it must be appreciated that this has implications for government's capacity. Infrastructure projects have traditionally been funded by the public sector in Pakistan in the past. The government has some level of experience with PPPs through engagement in this mode with Independent Power Producers (IPPs) in the 1990s; PPPs have also been used in the past in the transport sector using the Build Operate Own, Build Operate Transfer, Rehabilitate Operate Own and Rehabilitate Operate Transfer modalities of engagement. However, in order to undertake major infrastructure projects in the PPP financing mode, transformation of the government's capabilities and governance capacities is needed to plan, execute and implement.

The government must therefore plan to enhance its institutional competencies in the area.

Fortunately, some arrangements are already in place but need critical inputs, consolidation and or transformation. A PPP policy is in place at the federal level but legislation needs to be enacted. A draft PPP law has been pending action in Punjab for over five years and needs to be built upon further to develop a national legislative framework. Steps have been taken to develop transaction advisory capacity—IPDF has been created as a statutory entity under the Companies Ordinance (as a Section 42 Company) to provide technical oversight, help state agencies procure transaction advisors and technically support government agencies in processing and developing projects through the PPP route. It is important to ensure support to the organization from the highest level of government to enable it to serve its role. In order to ensure availability of long-term financing for PPPs, various financing arrangements—Viability Gap Fund, the Guarantee Fund, Infrastructure Project Finance Facility and Project Development—have been designed for some time now but have not been fully established. The PPP infrastructure Cell in the Planning Commission also needs to be supported and strengthened to plan and procure infrastructure with private sector investment. This arrangement with appropriate linkages and technical inputs from IPDF can be mandated to review all infrastructure projects for their viability regarding being channeled for private sector funding before going down the CDWP/ECNEC route in the Planning Commission. In many countries of the world, it actually has to be proved that infrastructure cannot be built with private sector investment before soliciting support for public financing such as is the case in South Africa and the highway sector in India.

An important caveat relates to capacity of the government to regulate. Infrastructure PPP's are complex arrangements involving a range of stakeholders—public companies with official relationships with public institutions, transaction advisors that are procured by public agencies (IPDF in Pakistan's case), operators, service purchasers, sponsors and

contractors; there are various sources of cash flows and revenues and organizational objectives that have to be handled. In view of this diversity and complexity, the success of these arrangements depends upon fiscal and legal prudence of governments and their ability and transparency to build safeguards and share risk in a manner that is mutually beneficial, both to the public and private sectors—most importantly, to the population at large.

The other reason why the government needs to engage with the private sector is to enhance its capacity to deliver social services—health and education in particular. Pakistan has traditionally engaged in service delivery in a ‘welfare mode’ assuming that it bears the responsibility, both of financing as well as providing services but has under-resourced its infrastructure and service delivery arrangements; on the other hand, the regulatory environment has allowed burgeoning of the private sector in these areas with minimal—in some cases no—regulatory controls. As a result of this and the disparity in incentives in the public vis-à-vis the private sector, a characteristic abnormality has emerged; this manifests itself in public functionaries working in the private sector, and closed and underperforming health facilities and schools. This limits the ability of the government to target welfare to its citizens.

In order to address these challenges, action is required at several levels—in each, the role of the private sector is critical. In order to better manage public facilities, the government can rely on the private sector’s entrepreneurial talent either by contracting out management or applying private sector management principles and incentivize public sector delivery and in order to expand the outreach of services, the government can involve non-state providers of services. The decision by governments to act as payers for welfare services and only partly have responsibility for direct delivery of services has important consequences for

shaping a social policy. However, the government will have to develop a new set of institutional norms and regulatory frameworks and change the way they have been doing business in the past in order to achieve this important goal.

The discussion on infrastructure development and sustainable macroeconomic growth and effective targeting of welfare service becomes more important and challenging today than it has ever been in the past in view of the unique pattern of conflict and violence that has emerged in our deeply polarized environment. The need to maximize synergies between the public and private sectors has therefore become an imperative. However, the results of such actions will only be as good as governments can make them. Governments with limited capacities cannot remedy their deficiencies by seeking to yoke the private sector on their own uncertain cart.

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