Pathfinder Economic Flash

SOE Losses: Negative Consequences for People, Employees & the Political Leadership

Recent media headlines have featured large losses incurred by state-owned enterprises (SOEs). CPC, CEB, SLTB and Sri Lankan Airlines/Mihin Air have all recorded unsustainable losses. A very large share of these losses, particularly those of the CPC, CEB and SLTB, can be attributed to pricing policies that do not reflect costs.

Over the past 35years, this practice has been sustained by very generous levels of foreign aid (grants and concessional loans) received from donors. This well-intentioned support had the perverse effect of encouraging successive governments to continue with populist policies and avoid taking the hard decisions that are necessary to ensure the country lives within its means.

As mentioned in several previous Pathfinder Foundation (PF) Economic Alerts and Flashes, we can no longer continue to live beyond our means now that we are a lower-middle-income country and no longer have access to concessional financing. In the last couple of years, the Government has been able to substitute external commercial borrowing for foreign aid. However, the headroom for this is no longer available, as reflected in the government's prudent decision not to undertake any further commercial borrowing in 2013.

In the circumstances, there is now no option but to operate SOEs, particularly the CPC and CEB, on a break-even basis. This can only be done by increasing the prices of fuel and electricity. However increasing prices on their own will merely impose a burden on the people by increasing the cost of living and also erode the competitiveness of local businesses.

Hence while price increases are necessary and eventually inevitable, they need to be accompanied by other structural reforms that increase efficiency and boost business confidence. Without this, the economy will be trapped in a downward spiral. PF has repeatedly called for such reforms. They are repeated yet another time.

Effective SOE reform is extremely unlikely without creating competitive structures where there are monopolies currently. The successful experience with the Telecommunications sector is ample testimony to this. Other structural reform could include the following: PPPs for maintaining the momentum of infrastructure development; further implementation of the recommendations of the Tax Reform Commission; a rigorous public expenditure review, including better design and targeting of subsidies and transfers; land and labour market reforms; tariff reform; further improvements in the investment climate; and confidence-building regarding the consistency and predictability of policies, including the sanctity of contracts and the rule of law in the commercial sphere.

There are many losers associated with loss-making SOEs: the consumers who ultimately bear the costs and receive poor quality services; the employees who are under-employed in low productivity jobs that are poorly paid; and political leaders who are often blamed for the poor quality of services and are rightly or wrongly tainted with perceptions of corruption.

At the end, the PF wishes to ask: 1. shouldn't our priority be the consumer interests i.e. high quality and reasonable price? 2. Why can't the policy makers and the political leadership learn lessons from the Telecom sector reforms (privatizing and de-monopolizing) which resulted in high quality services, affordable prices and innovation?

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