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Privatization: Is Dismantling Public Authority an International Trend?

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Abstract

Despite recent government bailouts of private industry, stimulus packages, and state-led restructuring of companies, economic and academic trends toward privatization continue, with public opinion generally supportive or neutral toward privatization. It is important to realize that privatization does not necessarily imply the dismantling of public authority. Privatization and nationalization can and do coincide, and it is likely that we will see more of both in the near future.

Is there an international trend toward privatization? If there is, will it be reversed by the present economic crisis? Those are the questions I intend to address, knowing that the typical economic prediction is no more precise than next week's weather forecast. But given that scientists are now discussing the climate on this planet 100 years into the future, I hope that you forgive me for trying to guess how the process of privatization will develop internationally for the next couple of years.

It is safe to say that privatization has notable economic consequences. The process of privatization is usually defined as the transfer of firms or assets from government to private parties. The outsourcing of publicly financed services to private companies is also sometimes loosely referred to as privatization (e.g. in Sweden and in the US). Privatization and public sector outsourcing have in common that direct public authority and control over an area is dismantled in favor of indirect methods of governance. Whether privatization is good or bad news from a citizens' rights perspective, will depend on how authority is used and misused in the public and in the private sector. In any case, privatization is problematic if it gives rise to a situation in which public authority is exercised over private companies at the expense of transparency and accountability. When a publicly financed service is outsourced to a private company, it is typically still the local politicians – and not the company delivering the service – who are ultimately held accountable by the political system.

Is privatization, then, an international trend? I will give three answers by looking at three trends of privatization: Economic, academic, and public opinion trends. By using three trends I hope to reduce some uncertainty when discussing the future of privatization. And if this future, just like oftentimes the weather, turns out differently than forecasted, we will at least know something about the reasons for the deviation. For our purposes, I will examine the trends in an international perspective.

An economic trend

Is privatization an economic trend? The quick and easy answer is yes. It all started in the early 1980s when Britain's government, under Prime Minister Margaret Thatcher, started to sell state-owned companies on a large scale. During 18 years of conservative government, the share of state-owned firms fell from 11% to below 2% of GDP. Since then, the idea has spread from country to country, from the privatization of previously nationalized banks in France in the mid 1980s to wide-ranging sales of companies in Nigeria in the past four years. Together with several other European countries, Canada, Chile, Jamaica, Japan, Malaysia, Singapore, and the United States privatized companies through public share offerings in the 1980s.¹ Sweden joined

¹ Megginson (2005), p 17.

the movement at the end of the 1980s, and the government sold its last shares in Swedish Steel Corporation (SSAB) in 1992.

In the 1990s, privatization spread across the globe with plenty of direct asset sales in Latin America, Africa, and South Asia. Additional European countries also launched privatization programs, most notably Italy where the large state holding company IRI has now been fully dismantled. In Latin America, the privatization programs in Brazil, Chile, and Mexico were particularly large and influential. The collapse of communism transformed firm ownership in central and Eastern Europe through massive and rapid privatization programs. Since 2000, privatization has been volatile, with a downturn in 2001–2003. It is only to be expected that the attractiveness of selling state-owned companies varies with their valuation on the stock market. Nevertheless, several important privatization deals have taken place in Asia (mostly in China, Japan and Korea). As shown in Figure 1, the worldwide revenues from privatization have recovered quite quickly from the poor years of 2001–2003. As Figure 2 shows, privatization has been a global phenomenon, although concentrated in East Asia, the Pacific, Eastern Europe, and Central Asia.

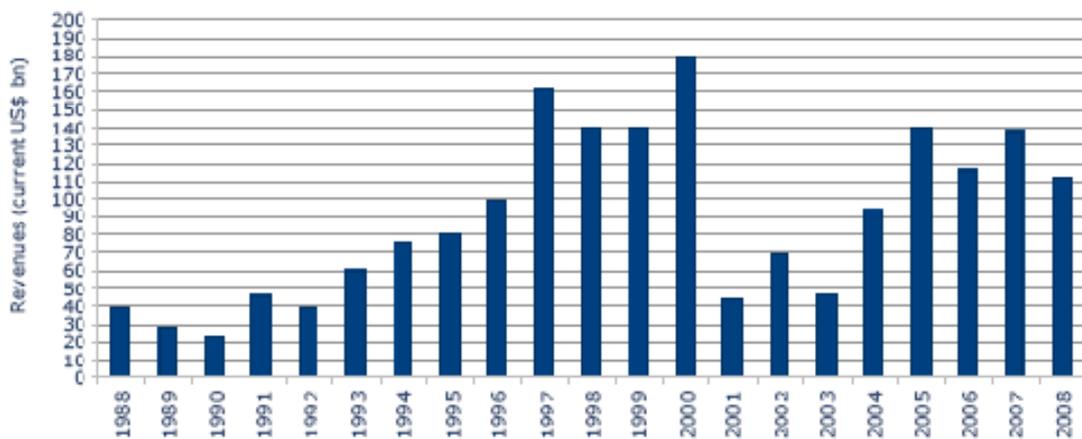


Figure 1: Worldwide revenues from privatization 1988–2008

Source: Privatization Barometer.

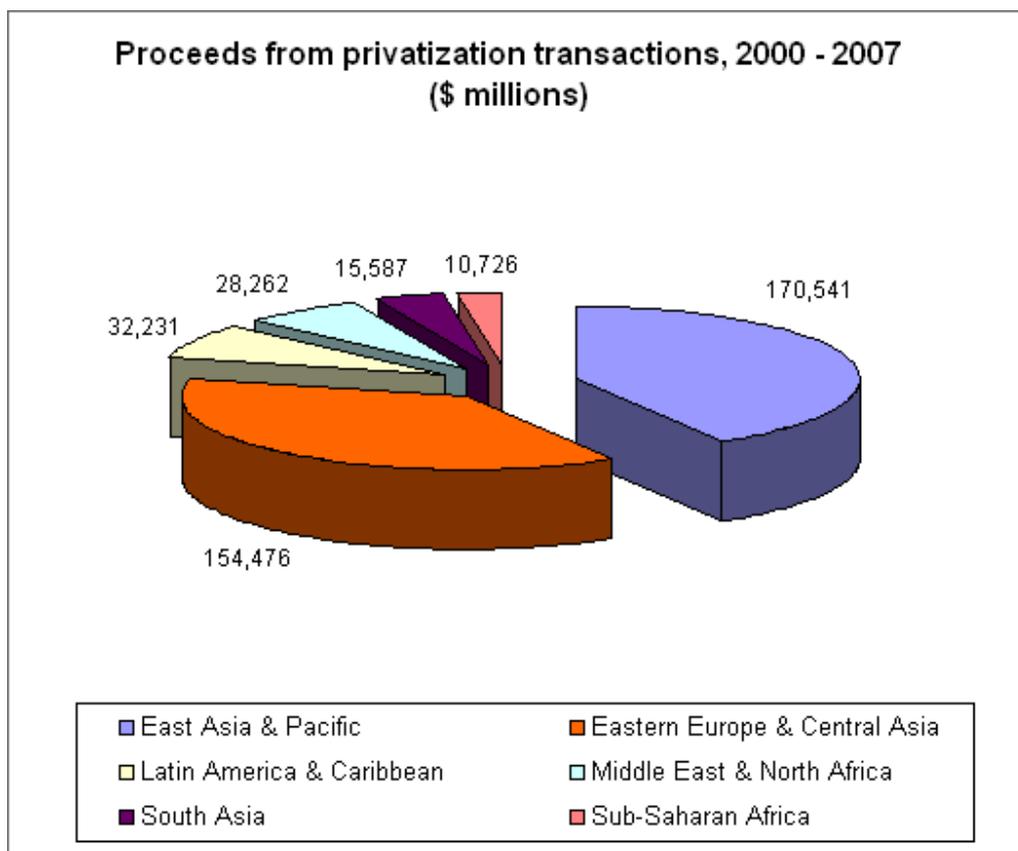


Figure 2. Privatization proceeds
Source: World Bank Privatization Database.

A tougher question is whether the present economic crisis will lead to a turning point for privatization. At first glance, Figure 1 suggests that the answer is “no.” Worldwide privatization revenue declined in 2008 but still totaled \$110 billion and exceeded \$100 billion for the fourth year in a row. Compared with the bust right after the turn of the millennium, governments were not that reluctant to sell state-owned companies in 2008 – although several planned privatizations were put on hold or cancelled. With this in mind, one can argue that the relative stability of privatization revenue during the present economic crisis indicates that share-issue privatizations could increase dramatically once financial markets have stabilized.

But the revenues from privatizations during the ruinous year of 2008 do not tell the whole story. This was the first year since the nationalizations in 1981 by France’s government, headed by Francois Mitterand, that saw the governments of the world acquire more assets from the private sector than they divested. And again the banks were at center stage. The 2008 acquisitions of bank stocks and loans probably exceeded an astonishing \$1.5 trillion, which is

about equal to the accumulated privatization revenues in the world since 1977.² Governments in the U.S., U.K., Germany, Ireland and other countries are suddenly sitting on enormous bank assets. This means that whether and when banks will be re-privatized will be decisive for the trend of privatization in the future.

In 2009, we have already seen the creation of “Government Motors.” After bankruptcy and reorganization, the U.S. government will own 60% of General Motors, in return for \$50 billion of taxpayers’ money. At present, the Chrysler case appears similar, albeit less dramatic, with \$10 billion in federal aid and a minority stake held by the U.S. government.

All in all, privatization has been an international economic trend. Whether recent bailouts, stimulus packages, and state-led restructuring of companies signal a turning point has yet to be seen. Before offering some predictions, I would like to examine privatization as an academic trend and as a trend in public opinion.

An academic trend

Knowledge matters. Researchers should deal with issues of policy relevance, so that policy makers can consult the latest findings before casting votes and taking action. As long as an idea receives serious scholarly attention, it will merit consideration on someone’s political agenda. Figure 3 shows that academic studies of privatization took off in the 1980s and have remained at a high and slowly growing level since the beginning of the 1990s. The figure is based on the Social Sciences Citation Index of Thomson Reuters, and privatization dominates most other notable public policies in this index, including welfare reform (by a factor of 3), minimum wages (by a factor of 8), and central bank independence (by a factor of 17).

These numbers obviously give no assessment of privatization, but economic studies that provide support for privatization outnumber opposing studies 6 to 1, according to a World Bank report.³ And going from quantitative to qualitative findings, recent reviews of the economics literature strongly support privatization in competitive sectors and – depending on regulation – also in many less competitive sectors.⁴ When reviewing the empirical evidence in OECD countries for the Swedish government, I concluded that state-owned companies tend to become more efficient and profitable after being privatized.⁵ In academia – and definitely

² Privatization Barometer (2008, p 3).

³ Shirley and Walsh (2001).

⁴ See Megginson and Netter (2001), Sheshinski and López-Calva (2003), and Megginson (2005).

⁵ Jordahl (2009).

among economists – there is still a trend in favor of privatization, and this is a possible determinant of privatization programs in the future.

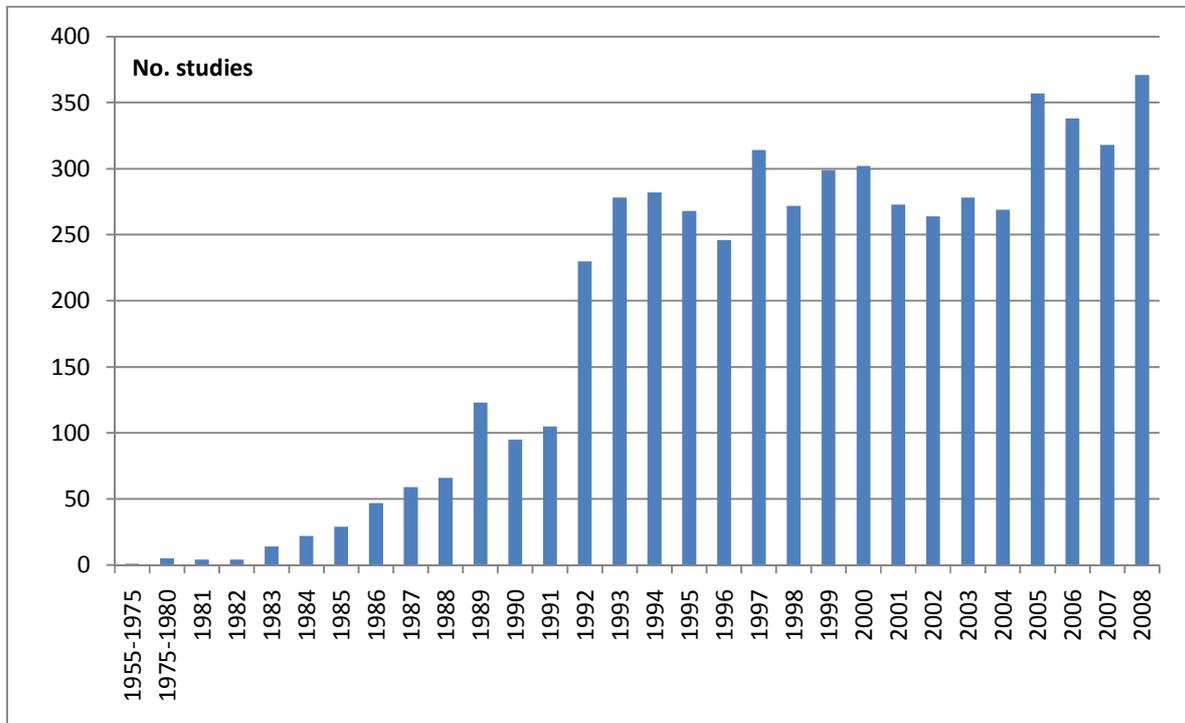


Figure 3. Privatization in the Social Sciences Citation Index

Note: Search results of the queries "privatization" or "privatizations" in topic or title.

A trend in public opinion

A common observation is that privatization is not as popular among voters as among politicians. In any case, the fate of privatization will ultimately depend on its support in public opinion. Figure 4 shows that – with the exception of China and Japan – privatization (the opposite of increased government ownership) has become less popular worldwide between 1990 and 2005. Still, the average citizen in many countries (most notably in the U.S. and Canada) implicitly support further privatizations, although in most countries the average is quite close to the neutral position at the middle of the scale (5.5). Admittedly, as this internationally comparable data set is not yet available for more recent years than 2005, we don't know whether the trend has continued.

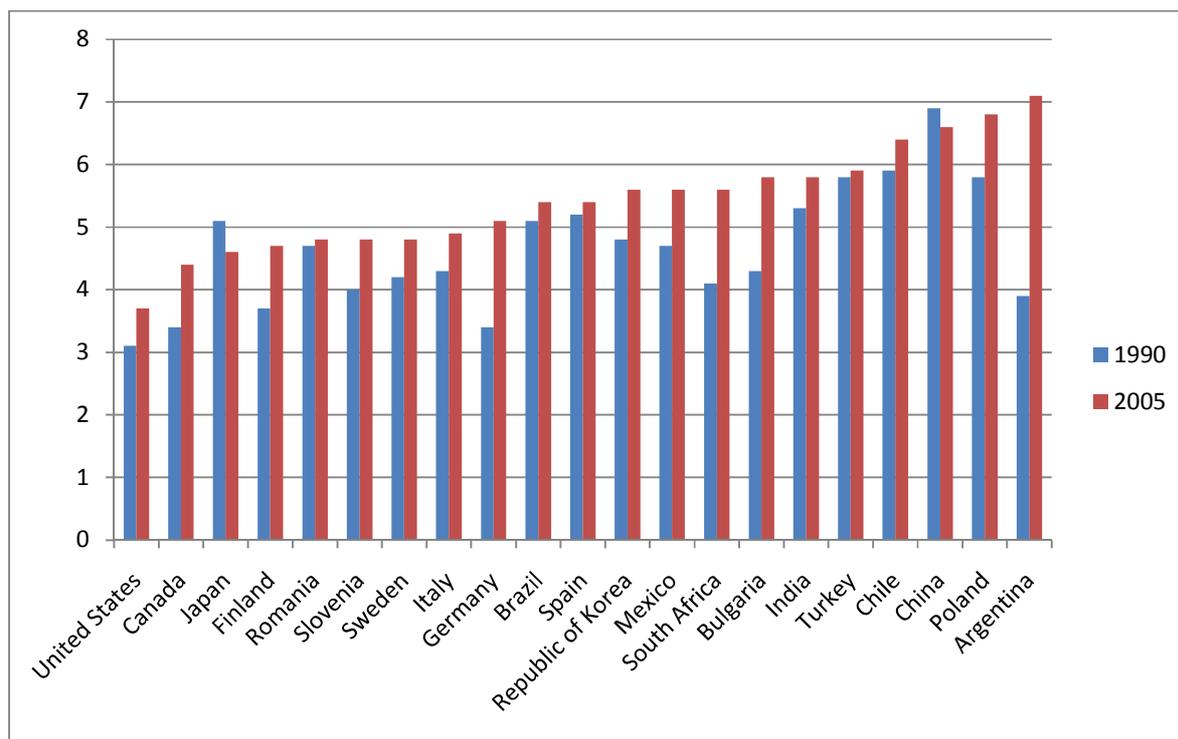


Figure 4. Average support for increased government ownership of business (1–10 scale)
Source: World Value Surveys.

To give a simple explanation of the falling, but on balance marginally supportive sentiments in favor of privatization has been difficult. Recent research points to country-specific determinants and also to the issue of whether support for privatization may be inseparable from wider predispositions toward markets in general.⁶ Generational differences may provide some guidance. Young people are generally more inclined to support state ownership over private property, except in former socialist countries where the generational divide is reversed and considerably stronger.⁷

Importantly, this means that privatization does not necessarily imply the dismantling of public authority. Privatization and nationalization can and do coincide. It is evident that governments did not see previous privatizations as binding and irreversible commitments.

About the long run, one can only speculate. Personally, I believe that countries will look for a leader and an example to follow. In the 1980s, Britain took the lead and the world followed her example. Today, our eyes are turned towards a different large-scale experiment in a bigger and

⁶ See e.g. Battaglio (2007).

⁷ Landier, Thesmar and Thoenig (2008).

more powerful country. What the Obama administration does and how these actions eventually turn out will influence and direct policymakers all over the world.

The current U.S. President, Barack Obama, has declared that he does not want to run an auto company. So what should he do now that his government essentially owns one? General Motors' new business plan prescribes a hands-off approach, temporary government involvement, and a strategy for exit. Recent political history, from Sweden and other countries, gives ample evidence that this is easier said than done. For years to come, the Cadillac will be a symbol of nationalization, of state ownership, and – if it does not run out of fuel – of privatization.

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