




PRIVATISATION AS A WORLDWIDE TOOL OF ECONOMIC REFORM: A LITERATURE REVIEW



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ABSTRACT

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This paper aims to present a general overview of the literature relating to privatisation as a worldwide economic phenomenon. It starts by describing the origins, definitions and the rationale for privatisation. The spread of the privatisation phenomenon throughout the world is also discussed. The study then provides justification for privatisation in less developed countries (LDCs). It also summarises privatisation objectives, the sequencing and pace of privatisation, factors influencing privatisation and the agent principal theory. The study then outlines the different privatisation methods and briefly refers to efficiency and effectiveness in the context of privatisation, privatisation and changes in corporate governance as well as arguments on privatisation. A discussion into the role of international agencies in the privatisation process is also provided and summarises the main lessons drawn from privatisation. Previous research including empirical studies comparing the performance of government owned companies, empirical studies in developed countries (non-transition economies), and in developing countries (transition economies) as well as empirical studies comparing pre and post privatisation performance changes are comprehensively discussed.

Contribution/ Originality: The significance of this research effort lies in the fact that researchers who are interested in investigating and studying privatisation can use this study to identify a promising directions for future research.

1. ORIGINS OF PRIVATISATION

Privatisation is not one clear and absolute economic proposition (see for example (Beesley and Littlechild, 1983; Park, 1997; Wright, 2002; Dawar and Ndlovu, 2017)). It means different things in different parts of the world, where both the fundamentals of the economy and the purpose served by privatisation may differ. Hence, it covers a wide range of activities, all of which imply a transfer of the provision of goods and services away from the public sector. For instance, privatisation is a somewhat new word. It made no significant emergence in political or economic literature before 1979. The word itself did not appear in the British Conservative Party's election manifesto of that year. However, it rapidly became one of the most significant policies of the 1980s, spreading outward from the UK to influence more than a 100 countries worldwide.

However, the term “privatisation” is widely believed to have first been used by Mr John Diebold, an American policy maker, who used this term during his campaign to transfer a government owned service from the public sector to the private sector in the USA (Lord, 1987). According to the Economist magazine the term “privatisation” appeared in print for the first time in the Economist in the early 1970s.

Privatisation can be considered as an umbrella term which can be used to denote a scale of policy initiatives in different countries with different modes and motives. The word “privatise” itself can be taken to mean the opposite of nationalise, i.e. as the transfer of ownership of state enterprises to the private sector. Privatisation can also be defined in simple terms such as “the process by which governments sell their state owned enterprises (SOEs), completely or in blocks of shares, to private investors, local and foreign”

Meggison and Netter (2001) document that privatisation as a political, social and economic policy can be taken to mean “the deliberate sale by a government of state-owned enterprises (SOEs) or assets to private economic agents”.

Overall, from the above definitions, privatisation can be described as a political, social and economic process, which leads to change in ownership structure of the enterprise from the state to the private sector. In addition, privatisation encourages the private sector to play a vital role alongside the public sector in reducing the level of government intervention in terms of planning, regulation and subsidies.

2. THE SPREAD OF THE PRIVATISATION PHENOMENON THROUGHOUT THE WORLD

Over the last four decades, there has been a widespread change of opinion regarding the role of state and private enterprises in promoting economic growth. Despite the fact that SOEs are the most common example of privatisation, it must be noted that governments can also privatise land, housing (which has been done in the UK) and even services and utilities such as banking, insurance, education, road construction, maintenance, water, electricity and other services that have been privatised in different countries by contracting out to private companies. More important than understanding privatisation itself as a process is understanding its underlying rationale that there are limits to what governments can provide and that some economic undertakings, especially industrial companies, are tackled more efficiently by the private sector. .

It was mentioned earlier that it was the UK that pioneered privatisation. It was the UK also which in many cases pioneered the growth of the state sector among private enterprise economies. It was undoubtedly British teaching which inspired many countries of her previous empire to follow the course of public sector economics and centralised planning.

It is hard to find a country that has not experienced privatisation of some kind or another. While the privatisation trend, historically, is usually associated with the UK, the first “denationalisation” programme occurred in the Federal Republic of Germany (FRG) in 1957, during the post war government of Konrad Adenauer. The first major sale occurred in 1961, when the FRG sold a majority stake in Volkswagen in a public share issue, and four years later orchestrated a similar secondary share issue for VEBA. These two issues increased the number of shareholders in Germany from approximately 500,000 to almost 3,000,000 (Meggison *et al.*, 1994).

After the UK, many different countries adopted privatisation programmes. Meggison *et al.* (1994) document divesting share issues by Denmark, Italy, Chile, Malaysia, and Singapore in 1985. The next major country to adopt privatisation was France, which marked a sharp break with the country’s dirigiste tradition of state intervention.

In addition, Austria, Belgium, Holland, Jamaica, Japan, Spain, Sweden, and the United State all implemented significant privatisation programmes through share issues during 1986 and 1987 (Meggison *et al.*, 1994). After 1987, privatisation programmes spread rapidly around the world, especially to developing countries in South America, Africa, and South Asia. Although most of these programmes depended heavily on private sales, the authors document significant share issues in Bangladesh, Brazil, Chile, Gambia, Malaysia, Mexico, Nigeria, Sierra Leone, Singapore, and Venezuela.

Since then, privatisation has developed largely as a robust economic policy tool to the extent that more than a hundred national governments have adopted at one degree or another. Indeed the relative universality and popularity of adopting privatisation programmes is because of the fact that privatisation can not only improve governments' performance but also generate vast amounts of revenue for governments without having to increase taxes or cut spending programmes (Levine, 1997; Boutchkova and Megginson, 2000).

According to Boubakri and Cosset (1998) "privatisation has turned into a major worldwide phenomenon, in both developed and developing countries. Over the last decade, privatisation of SOEs has been occurring at an increasing rate, especially in developing countries. The share of these in global privatisation revenues has risen from 17 per cent in 1990 to 22 per cent in 1996" and is expected to exceed 40 per cent by 2020 (Ismail, 2018).

3. PRIVATISATION IN LESS DEVELOPED COUNTRIES (LDCS)

Privatisation with economic, political and social objectives and strategies is a relatively new experience for the developing countries of the world. Essentially, privatisation is a response to the domestic, economic and political situations of these countries. In fact privatisation has been prescribed as a method for improving the operating efficiency and thus profitability of public enterprises (PEs). "Although it is often claimed that the privatised company will achieve a higher return on capital invested and will accelerate economic performance, their generally poor profit performance or discounted cash flow and heavy debts have raised many doubts about their economic efficiency in generating surplus capital for developing countries" (Cowan, 1983).

It has even been suggested that in some developing countries, public enterprises have become a vehicle of corruption, nepotism, misappropriation of public funds and indeed an instrument for furthering the political and material interests of ruling parties. Nevertheless, these views are generally applicable only where public enterprises experience a high degree of political bureaucratic interference in commercial decision making. Reviewing the literature in this context has revealed that public enterprises have not been able to accomplish their objectives particularly well in developing countries. Accordingly, the privatisation process in developing countries could be justified in order to overcome the above mentioned problems.

4. PRIVATISATION OBJECTIVES

The literature review shows that privatisation objectives are broadly similar across countries in that they concentrate on achieving benefits from re-balancing the roles of the private and public sector to enhance the productive power of the economy. Hence, the major objective of privatisation is to develop the private sector and introduce regulatory reform in the public sector in order to improve efficiency, generate revenue or profits, create employment opportunities, improve the quality of services and develop capital markets.

The specific reasons behind privatisation at a national level are varied and inter-linked. The objectives can be political, economic, fiscal, social or, most frequently, a combination of several of them. Among the reasons behind privatisation, as documented by UNCTAD (1995), Vickers and Yarrow (1993), Liebreman (1993) and Estrin and Pelletier (2018) are the following:

- 1- To promote economic efficiency by fostering well-functioning markets and competition.
- 2- To redefine the role of the state in order to allow it to concentrate on the essential task of governing.
- 3- To reduce government involvement in enterprise decision-making.
- 4- To promote the development of capital markets.
- 5- To encourage employee share ownership.
- 6- To reduce the fiscal burden of loss-making public enterprises, in order to help regain fiscal control and macroeconomic stability.
- 7- To reduce public debt and public sector borrowing requirement (PSBR).
- 8- To release limited state resources for the financing of other demands.

- 9- To generate new investment, including foreign investment, for instance in the area of education.
- 10- To mobilise domestic resources for development and deepen domestic financial development.
- 11- To spread and democratise share ownership.
- 12- To improve the generally unsatisfactory performance of SOEs through the discipline of private ownership.
- 13- To “turn around” or restructure sick SOEs.
- 14- To raise cash through SOEs sales, and
- 15- To increase exports.

5. RESTRUCTURING AND PRIVATISATION

Restructuring and privatisation are now widely considered as vital means of government policy to create suitable conditions for enhanced economic growth and for redefining the role of the state. There are a large variety of restructuring and privatisation models of state utilities, ranging from minimum to full withdrawal of the state. Moreover, restructuring most likely leads to privatisation, its goal being to make companies more attractive to potential buyers and operators.

Theoretically, many scholars have tried to answer the questions of when to privatise, whether to privatise rapidly or slowly, what order should be followed in privatising companies (sequencing), whether a SOE should be sold at once or in stages (staging), and whether a SOE should be restructured prior to sale (or just restructure SOE) (Megginson and Netter, 2001). In this respect, many authors have modelled the matter of both the sequencing and staging of SOE sales (such as Boycko *et al.* (1996)). The models explain the importance of sequencing and staging by the privatising government to build reputational capital with investors and create local support for the privatisation programme. On the other hand, these complex relationships have decreased researchers’ ability to identify factors in sequencing and staging.

It is now generally agreed that privatisation and restructuring do not produce the same outcomes in all places, and their design and implementation need full preparation as well as considerable consultation. These processes do not necessarily lead to more efficiency, greater competition or a more profitable operation, and should be developed in a larger context of market reform, bearing in mind standards of good management and competition regardless of the structure of ownership,

6. AGENT-PRINCIPAL THEORY, OWNERSHIP AND COMPETITION

Agency situations occur when one party (principals, such as shareholders) delegate to another party (i.e. agents, such as managers) decisions over the use of their property or property rights (Arrow, 1985; Martin and Parker, 1997). This arrangement may be economically efficient from the point view of specialisation or comparative advantage, but agency relationships also include the idea of divergent objectives. The schedule of the agents may not be the same as those of the principals, particularly because agents can be expected to be self-interested. In particular principals are at risk from the dysfunctional behaviour of agents, which then decreases the value of the property rights (Martin and Parker, 1997; Abdeldayem, 2015). The possible impact of both the product and capital markets on performance is illustrated in Table 1.

Table-1. Alternative ownership and competitive regimes.

	Monopoly	Competition
Public ownership	A	B
Private ownership	C	D

Source: Martin and Parker (1997).

Martin and Parker (1997) developed an economic model in which improvement in economic performance relies on ownership, competition and managerial freedom. They suggest the following hypotheses:

- 1- *D* is superior to *A*, where “*D*” represents private ownership and a competitive market and “*A*” has public ownership and a monopolistic market.
- 2- *D* is superior to *C*, since “*C*” represents a private monopolistic market. This reflects the standard economic view, which prefers a competitive market.
- 3- *D* is equal to or superior to *B*. This implies that in a competitive environment private companies are better than public companies.
- 4- *B* is superior to *A*, indicating in a non-competitive environment the policy role of a private capital market.
- 5- *B* is superior, inferior or equal to *C*, depending on the ownership role as well as the monopolistic position.

The expectation is that maximum efficiency gains can be achieved if privatisation is combined with a kind of competition in the product market, this might occur in the case of moving from point “*A*” to “*D*”. Smaller gains might be expected when the movement is from point “*A*” to “*C*”(i.e. privatising a monopolist) or from “*B*” to “*D*” (i.e. privatising a company in a competitive market). Gains might also be expected when the movement is from “*A*” to “*B*” (i.e. exposing a publicly owned monopoly to competition) or from “*C*” to “*D*” (i.e. exposing a privately owned monopoly to competition).

As far as agency theory is concerned, a standard property rights approach to public and private ownership documents that there are agency problems in all forms of ownership, but since ownership is transferable through competitive capital markets in the private sector, a better use of resources can be achieved. On the other hand, public choice theory is concerned more directly with actual behaviour in the public sector. At the core of this literature is a big debate over how much politicians and state bureaucrats follow their own agendas rather than the public interest (Aranson, 1990; Martin and Parker, 1997; Abdeldayem, 2015).

7. METHODS OF PRIVATISATION

The decision of selecting the method of privatisation to be adopted is a difficult one since this decision includes some economic factors such as valuing the assets as well as some political aspects. However, Megginson and Netter (2001) highlight that several factors that affect the privatisation method should be taken into consideration. Of these factors there are:

- 1- The history of the asset’s ownership
- 2- The financial and competitive position of the SOE
- 3- The government’s ideological view of markets and regulation
- 4- The past, present, and potential future regulatory structure in the country
- 5- The need to pay off important interest groups in the privatisation
- 6- The capital market conditions and existing institutional framework for corporate governance in the country
- 7- The government’s willingness to let foreigners own divested assets

Therefore, the complexity of the objectives of the privatisation process means that different countries have used many different methods or techniques in divesting many different assets. According to Brada (1996) and Megginson and Netter (2001) there are four different categories in privatisation. Moreover, many privatisations use combinations of these different types of privatisation. These categories involve:

1- Privatisation through restitution: This method of privatisation is suitable when easily identifiable assets such as land which was expropriated previously can be returned either to its original owners or heirs. This method of privatisation is generally encountered mainly in Eastern European countries. The main difficulty with this method of privatisation is that it needs records to prove the ownership and these records could be unavailable or conflicting and inadequate.

2- Privatisation through sale of state property: According to this method governments trade their ownership claim for an explicit cash payment. This category includes two different methods i.e.:

2/a- Direct sales (or asset sales) of SOEs (or some parts of them) to an individual, corporation or a group of investors.

2/b- Share issue privatisations (SIPs), under which some or all of a government's stake in a SOE is sold to investors via a public offering of shares. These are similar to the initial public offerings (IPOs) in the private sector, but while private IPOs aim basically at increasing revenue, SIPs aim at raising money and responding to some political factors.

3-Mass or voucher privatisation: Under which eligible citizens can use vouchers (that are distributed free or at nominal cost) to bid for stakes in SOEs or other assets that have been divested. This method has been adopted only in the transition economies in Central and Eastern Europe.

4-Privatisation from below: This method of privatisation became more popular in the former socialist countries as well as several transitional economies. Rapid entry and formation of new business has been a feature of nearly all transitional economies. Growth of the new private sector is widely recognised as one of the success stories of the economic transition from socialism. The key feature of this method is entry, which creates competition and drives market development, leading to a decline in state control and monopoly.

In addition to the four categories mentioned above, there are other methods that governments can employ to increase private sector participation. For instance, [Vuylsteke et al. \(1988\)](#) highlight seven methods of privatisation, which are:

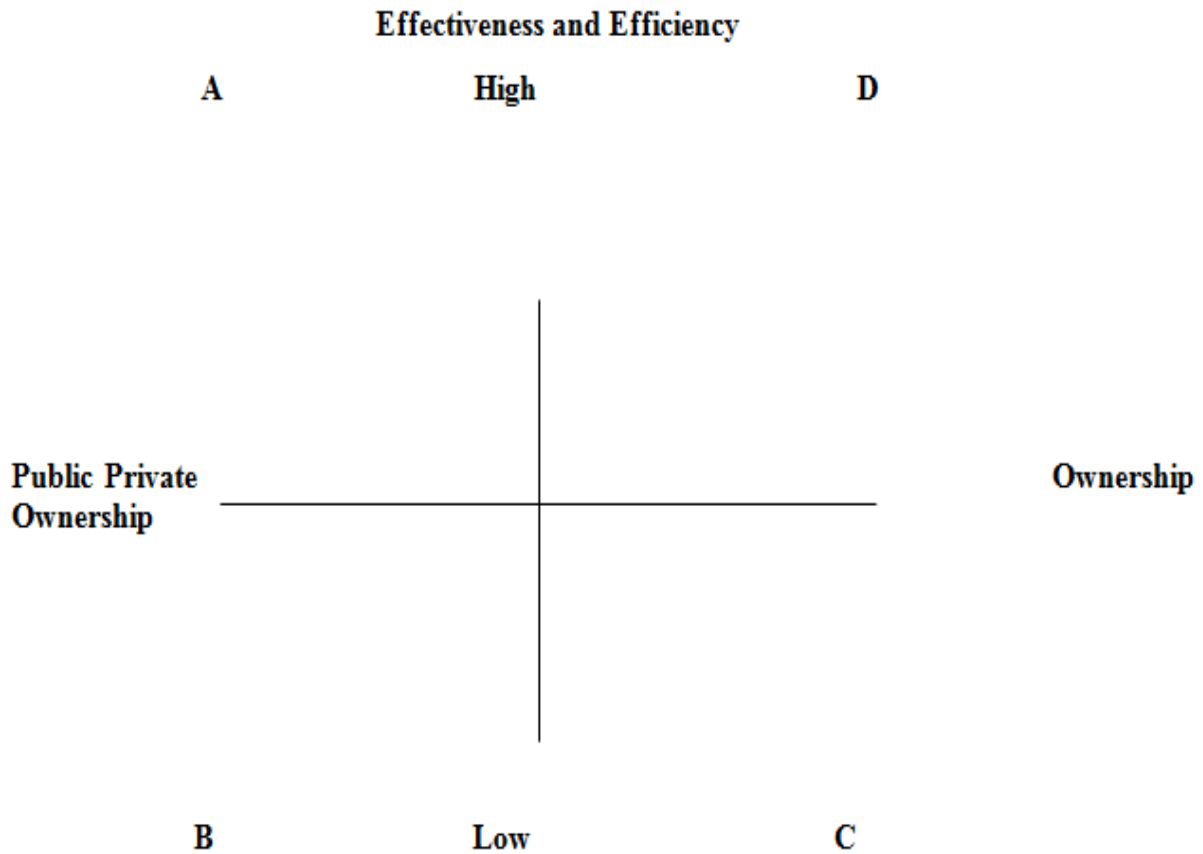
- 1- Public offering of shares (full or partial)
- 2- Private sale of shares
- 3- New private investment in an state owned enterprise (SOE)
- 4- Sale of government or SOE assets
- 5- Reorganisation (or break-up) into component parts
- 6- Management/ employee buyout
- 7- Lease and management contract

In the case of full privatisation, the government may sell the whole enterprise (i.e.100% of the enterprise shares) to the private sector. But if for political or other reasons the entire sale is not feasible, the government can then sell part of the enterprise and retain the majority of the shares (more than 50%), or a minority of shares. The sale of public enterprises, wholly or in part, does not have to occur in the market place. For instance the government might sell an enterprise to the employees of the enterprise. Another alternative is to sell a certain percentage of shares to the general public and retain the rest for the employees.

8. PRIVATISATION EFFICIENCY AND EFFECTIVENESS

[Vickers and Yarrow \(1993\)](#) argue that privatisation of a company, which enjoys substantial market power will tend to improve internal efficiency. However, this could be at 'the risk of allocative efficiency' unless a suitable framework of regulation and competition controls profit-seeking behaviour.

In this regard, [Hodges \(1997\)](#) argues that privatisation does not necessarily improve efficiency, effectiveness or service. A main advantage of the privatisation process is the removal of industries and companies from government intervention and the public financing cycle. The process has revealed that companies can be transferred while still publicly owned. Utilising a four-quadrant figure ([Figure 1](#)) ([Hodges, 1997](#)) reported that privatisation rhetoric has implied that companies will move from quadrant *B* to quadrant *D*, but in some cases the movement is from *B* to *D* via *A*. It is possible also that the move will appear as one from quadrant *B* to *C*, as there is no obvious relationship between economic/financial performance and managerial performance.



Source: Woodward (1990).

Figure-1. Privatisation and Effectiveness.

It is highly likely that escape from short-term political intervention will improve a manager's long term investment decisions and technical validity. However, in the case of actual or quasi-monopolies, where competition is limited, there is no certainty of improvement in effectiveness, efficiency and quality (Hodges, 1997; Shaker and Abdeldayem, 2018).

9. ARGUMENTS ON PRIVATISATION

There are many opponents to privatisation just as there are many advocates. As one of those who argue against privatisation, Thompson (1986) points out that privatisation:

- 1- Can give rise to private monopoly
- 2- Can lose track of the public interest
- 3- Could endanger the continuity, efficiency, and quality of service provision
- 4- Can lead to no democratic control and no possibility for citizen to directly address issues
- 5- Makes it more difficult to safeguard the interests of weaker groups in society
- 6- The market economy is not necessarily better than the public sector
- 7- May lead to financial disadvantages.

On the other hand, there are benefits that can result from privatisation. These are reported by researchers such as Pirie (1988); Mulley and Wright (1986) and Grimestone (1988) as:

- 1- Efficiency gains
- 2- Enhanced sensitivity to market forces
- 3- Enhanced flexibility, efficiency, and responsiveness by the government
- 4- Separation of power

- 5- Increased independence of organisations
- 6- Positive fiscal impact of privatisation
- 7- Wider share ownership or popular capitalism

In light of the above, the following criteria should be observed (1) privatisation is a cost benefit exercise, (2) it should be accompanied by competition and deregulation, (3) governments should solve the noncommercial objectives of SOEs, (4) as well as the financial disadvantages of privatisation and finally, (5) governments should create a great interest group in privatisation.

10. THE ROLE OF INTERNATIONAL AGENCIES IN THE PRIVATISATION PROCESS

International agencies such as the World Bank were affected by the policies of both the USA and the UK in the early 1980s. The World Bank adopted the policy of tackling poverty in the world, hence, the bank decided that markets should be as free as possible. Since then, much of the world's bank lending has been in the form of sector adjustment loans to European, Asian, Latin American, Middle Eastern and African countries. Between 1981 and 1992 the World Bank supported more than 70 countries with 182 operations, the majority of them in Sub-Saharan Africa, Latin America and Eastern Europe. After that, privatisation became a vital component of the Structural Adjustment programme (SAP) of the World Bank. The World Bank provides structural adjustment loans (SALs), sectoral adjustment loans (SECALs), technical assistance loans (TALs) and public enterprise reform loans (PERLs). During the last decade the bank has given these loans to many developing countries in the world in order to develop and accelerate their structural adjustment programmes as well as privatisation. In addition to the World Bank, there are some other major international donor agencies such as the International Monetary Fund (IMF), the US Agency for International Development (USAID), the International Finance Corporation (IFC) and the Asian Development Bank (ADB). All these agencies are involved in encouraging privatisation programmes, and finance, consultancy and advisory services to enhance reform programmes throughout the world (Ramamurti, 1997).

To conclude, both the major international agencies i.e. the World Bank and the IMF have turned towards the development of privatisation and this could be as a result of the impact of neo-liberal governments in industrialised countries.

11. PREVIOUS EMPIRICAL RESEARCH

Since privatisation became an essential part of government policy almost two decades ago, enough time has passed to allow researchers to undertake studies that examine the effect of privatisation on the financial and operating performance of former SOEs. Table 2 below lists 42 selected studies, which represent a summary of previous research work. These studies are discussed in more detail following the table.

To begin with, Boardman and Vining (1989) examined the financial execution of 500 of the biggest non-US organizations in 1983, characterized by the structure of possession as, state claimed, exclusive and blended proprietorship ventures (ME). They resort to four gainfulness proportions and two proportions of effectiveness. The creators report that state possessed and blended proprietorship organizations are fundamentally less gainful and profitable than exclusive firms. They additionally locate that blended possession organizations are not any more productive than state claimed firms. In this manner, unadulterated private possession is required to pick up productivity.

Vining and Boardman (1992) examine whether possession "matters" in deciding the productivity of state claimed endeavors (SOEs), or if just the level of rivalry is essential. The gauge execution display utilizes information from 500 of the biggest non-money related Canadian firms in 1986 (these organizations incorporate 12 SOEs and 93 blended possession undertakings). The creators, subsequent to taking into consideration a few factors, for example, a company's size and piece of the overall industry, locate that privately owned businesses are more

beneficial and productive than MEs and SOEs, and that MEs out-perform SOEs. In this way, proprietorship has an effect extraordinary and separate from rivalry.

Table-2. List of previous research work.

Study	Focus
(1) Boardman and Vining (1989)	Economic performance of 500 of the largest non-US companies related to ownership structure in 1983.
(2) Vining and Boardman (1992)	Effects of ownership and competition on SOE efficiency using data from 500 of the largest non-financial Canadian firms in 1986
(3) Pinto <i>et al.</i> (1993)	Improvement in SOE performance through privatisation by testing the response of the Polish state sector in the 1990s.
(4) Ehrlich <i>et al.</i> (1994)	Effect of state ownership on company performance for 23 international airlines during the period 1973 to 1983.
(5) Galal <i>et al.</i> (1994)	Post privatisation performance comparison of 12 companies from Chile, Malaysia, Mexico and the UK.
(6) Megginson <i>et al.</i> (1994)	Pre and post privatisation performance comparison of 61 firms from 18 countries and 32 industries during the period 1961 to 1990.
(7) Martin and Parker (1995)	Post privatisation performance comparison of 11 British companies' privatised between 1981 and 1988.
(8) Ramamurti (1996)	Privatisation programme study survey in Latin America between 1987 and 1991.
(9) Petrazzini and Clark (1996)	Effects of deregulation and privatisation on performance in 26 developing countries.
(10) Barberis <i>et al.</i> (1996)	Effects of deregulation and privatisation on performance in 452 Russian shops privatised during the early 1990s.
(11) Macqueira and Zurita (1996)	Pre and post privatisation performance comparison of 22 Chilean firms privatised between 1984 and 1989.
(12) Majumdar (1996)	Effects of different ownership structures on performance in India between 1973 and 1989.
(13) Boles de Boer and Evans (1996)	Effects of deregulation and privatisation on performance in New Zealand in 1990.
(14) Pohl <i>et al.</i> (1997)	Effect of privatisation on company restructuring in 7 Eastern European countries from 1992 and 1995.
(15) Ramamurti (1997)	Post privatisation performance comparison of Ferrocarril Argentinos, the national railroad, in 1990.
(16) Claessens <i>et al.</i> (1997)	Effects of deregulation and privatisation on performance of 706 Czech companies between 1992 and 1995.
(17) Kole and Mulherin (1997)	Private versus partly government owned company comparison of 17 companies partly owned by the US government during World War II.
(18) La Porta and Lopez-de-Silanes (1999)	Post privatisation performance comparison of 218 Mexican companies privatised in 1992.
(19) Weiss and Nikitin (1998)	Effects of investment and ownership on 125 privatised Czech companies between 1993 and 1995.
(20) Boubakri and Cosset (1998)	Pre and post privatisation performance comparison of 79 companies from 21 developing countries that privatised between 1980 and 1992.
(21) Claessens and Djankov (1999)	Effects of management turnover on 706 privatised Czech companies during the period 1993 to 1997.
(22) Ros (1999)	Effects of privatisation and competition on company performance in 110 counties during the period 1986 to 1995.
(23) Frydman <i>et al.</i> (1999)	When does privatisation work? Evidence from Czech Republic, Hungary and Poland.
(24) D'Souza and Megginson (1999)	Pre and post privatisation performance comparison of 85 firms from 28 industrialised counties that are privatised from 1990 to 1996.
(25) Boubakri and Cosset (1999)	Pre and post privatisation performance comparison of 16 African companies that are privatised between 1989 and 1996.
(26) Dewenter and Malatesta (2001)	Pre and post privatisation performance comparison of 63 large, high information companies privatised between 1981 and 1994.
(27) Tian (2000)	Effects of different ownership structures on performance of 825 Chinese firms in 1998.
(28) Boylaud and Nicoletti	Impacts of liberalisation and privatisation on performance of telecom services in

(2000)	23 countries during the period 1991 to 1997.
(29) Frydman <i>et al.</i> (2000)	Pre and post privatisation performance comparison of 506 companies from Czech Republic, Hungary and Poland.
(30) Lizal <i>et al.</i> (2000)	Post privatisation performance comparison of Czechoslovak SOEs in 1991 and 1992.
(31) Black <i>et al.</i> (2000)	History of privatisation programmes in Russia.
(32) Wallsten (2001)	Impact of reforms on telecommunications in 30 African and Latin American countries during the period 1984 to 1997.
(33) Laurin and Bozec (2000)	Pre and post privatisation performance comparison of Canadian National in 1995.
(34) Harper (2000)	Post privatisation performance comparison of 554 Czech privatised companies between 1992 and 1994.
(35) Verbrugge <i>et al.</i> (2000)	Pre and post privatisation performance comparison of 32 banks in OECD countries and 5 banks in developing countries.
(36) D'Souza and Megginson (2000)	Pre and post privatisation performance comparison of 17 national telecommunications companies privatised between 1981 and 1994.
(37) Dewenter and Malatesta (2000)	Effects of different ownership structures on performance of companies in 500 largest non-US companies during 1975, 1985 and 1995.
(38) Karpoff (2001)	Effects of different ownership structures on performance of the Arctic between 1819 and 1909.
(39) Harper (2001)	Effects of privatisation on operating performance of 178 Czech companies that were in the first wave of voucher privatisation.
(40) Bortolotti <i>et al.</i> (2002)	The Financial and operating performance of 31 national telecommunication companies in 25 countries.
(41) Wright (2002)	The impact of divestment on firm performance of 132 UK quoted companies over the period 1985 to 1993.

Pinto *et al.* (1993) examine whether privatisation is needed to improve the performance of SOEs by testing the response of the Polish State sector during the three years after the "Big Bang" reforms of January 1990. These reforms tightened monetary and fiscal policy, and liberalised prices but did not involve privatisation. The authors find that even without privatisation, performance improved significantly because of a macroeconomic stabilisation package. Essentially, these improvements came about through the imposition of hard budget constraints and tight lending policies that were adopted by banks.

The World Bank commissioned a major study undertaken by Galal *et al.* (1994) which compares the actual post privatisation performance of 12 companies from four countries: Chile, Malaysia, Mexico and the United Kingdom. The authors document net welfare gains in 11 of the 12 cases, in addition, they did not find any cases in which workers showed an overall loss from privatisation. However, they reported 3 cases in which workers were become significantly better off.

Megginson *et al.* (1994) compare the pre- and post privatisation performance (both financial and operating performance) of 61 firms from 18 (12 industrialised and 6 developing) countries and 32 industries that adopted privatisation through public share offerings during the period 1961 to 1990. The authors document significant performance improvement in terms of an increase in sales, profitability, capital investment spending and operating efficiency without sacrificing employment security. Moreover, these firms dramatically decreased their debt levels and increased dividend payout.

Martin and Parker (1995) using two measures (ROR on capital employed and annual growth in value added per employee-hour) to examine whether 11 British companies privatised between 1981 and 1988 had improved profitability and efficiency after being privatised. The authors document that less than half the companies perform better after being privatised and that several improved before privatisation.

Ramamurti (1996) surveys four telecom, two airlines, and one-toll road privatisation programmes in Latin America between 1987 and 1991. Further, the author discusses expected economic issues, ideological opposition to privatisation and methods used to overcome bureaucracy. The author reports that privatisation is very positive for

telecoms, because of the scope of technology, attractiveness of offer conditions and capital investment, while productivity improvements for airlines and roads were much more moderate.

Petrazzini and Clark (1996) document the fact that both deregulation and privatisation are associated with dramatic improvements in level and growth of teledensity, however neither have any consistent effect on service quality. Furthermore, while deregulation is associated with increases in employment and a decline in prices, privatisation has the opposite impact.

Pohl *et al.* (1997) compare the extent of restructuring achieved by more than 6300 private and state owned companies in 7 Eastern European countries from 1992 and 1995. They use 6 measures to determine which restructuring strategy improved performance the most. The authors document that privatisation significantly raises the probability of restructuring and the likelihood that it will be successful.

Boubakri and Cosset (1998) compare the pre- and post-financial and operating performance of 79 firms from 21 developing countries that experienced full or partial privatisation during the period 1980 to 1992. The authors document significant increases in profitability, operating efficiency, capital investment spending, output, employment level and dividends. Furthermore, the authors document a significant decline in leverage after privatisation.

Frydman *et al.* (1999) compare the performance of privatised and state owned companies in the transition economies of Central Europe and ask the question “When does privatisation work?” They test the effect of ownership composition on the performance of 90 SOEs and 128 privatised firms in the Czech Republic, Hungary and Poland. The authors highlight that privatisation “works” but only when the company is controlled by outside owners.

D'Souza and Megginson (1999) compare the pre and post privatisation financial and operating performance of 85 firms from 28 industrialised countries that are privatised through public share offerings from 1990 to 1996. The authors document dramatic increases in profitability, operating efficiency, output, dividend payments and capital expenditure. Moreover, employment decreases, but not significantly.

Boubakri and Cosset (1999) examine the pre and post privatisation performance of 16 African companies that are privatised through public share offerings between 1989 and 1996. They also summarise 3 other studies in developing countries related to privatisation. The authors document significant increases in capital spending by privatised companies but insignificant changes in profitability, output, efficiency and leverage.

Tian (2000) studies the relationship between state shareholding and the corporate performance of 825 Chinese firms in 1998. 413 firms had some government ownership, 312 firms had none. The author documents the fact that “private” firms’ performance is significantly better than that of “mixed” firms. In addition, the author finds in general that corporate value decreases with state ownership, but rises after the state share drops below 45 %.

Boylaud and Nicoletti (2000) employ databases of market structure and regulation to examine the impacts of liberalisation and privatisation on productivity, quality and prices of telecom services in 23 countries during the period 1991 to 1997. The authors document the fact that in telecom services, both potential and actual competition caused improvements in productivity and quality, but they could not find any clear impact of privatisation.

Lizal *et al.* (2000) using data for 373 companies in 1991 and 262 companies in 1992, test the performance impacts of the wave of break-ups of Czechoslovak state owned enterprises on the subsequent performance of the master companies and their spin off. The authors document the fact that in 1991, there was an immediate positive impact on the profitability and efficiency of small and medium size companies and a negative impact for the larger companies. In 1992, the results were similar but not statistically significant.

Black *et al.* (2000) survey the history of privatisation programmes in Russia. While mostly descriptive, a large number of case studies are analysed. The authors document the fact that Russian privatisation programmes in particular have failed and have created a “kleptocracy”. Furthermore, they concentrate on the importance of encouraging managers to delegate in the process of designing privatisation programmes.

Verbrugge *et al.* (2000) examine offering terms and share ownership results for 65 banks which privatised either fully or partly during the period 1981 to 1996. They also compare the pre and post privatisation performance of 32 banks in OECD countries and 5 banks in developing countries. The authors find moderate improvement in OECD countries. Profitability, fee income, and capital adequacy ratios all increased significantly but the leverage ratio decreased significantly. They also, document large ongoing state ownership and dramatic early returns to initial public offering investors.

Wright (2002) examines the impact of divestment on company performance, utilising an unbalanced panel of 132 UK quoted companies during the period 1985 to 1993. The results suggest that divestment has a positive, significant and substantial impact in increasing the profitability of the vendor company. In addition, the author finds limited support for the view that the benefit from divestment is greater for larger and/or more diversified companies and companies operating with weak governance arrangements.

In light of the empirical studies mentioned above, the researcher can classify the 42 empirical studies into four distinct categories. These are:

- 1- Empirical Studies comparing the performance of government owned companies.
- 2- Empirical Studies in single country or single industry (Non-Transition Economy).
- 3- Empirical studies in Transition Economies (either Central and Eastern Europe or Russia and the former Soviet Republics).
- 1- Empirical Studies comparing pre and post privatisation performance changes.

1. Empirical Studies comparing the performance of government owned companies

These studies include: Boardman and Vining (1989); Vining and Boardman (1992); Pinto *et al.* (1993); Ehrlich *et al.* (1994); Majumdar (1996); Kole and Mulherin (1997); Dewenter and Malatesta (2000); Tian (2000) and Karpoff (2001). Megginson and Netter (2001) present some prospective problems in researching this area such as: lack of data and bad data, endogeneity, omitted variables and selection bias. Furthermore, they report two methodological difficulties, particularly in attempting to isolate the impact of ownership on performance:

- a- *In comparing SOEs to privately owned firms, it is very difficult to determine a suitable set of comparison companies or benchmarks with a limited private sector particularly in developing countries.*
- b- *In general, there are essential reasons why the government owns specific companies while others are privately owned, involving the degree of perceived market failure within the particular industry.*

2. Empirical Studies in single country or single industry (developed countries)

The studies in this category include: Galal *et al.* (1994); Martin and Parker (1995); Ramamurti (1996); Petrazzini and Clark (1996); Ramamurti (1997); Ros (1999); La Porta and Lopez-de-Silanes (1999); Wallsten (2001); Laurin and Bozec (2000); Boycko *et al.* (1996) and Wright (2002).

3. Empirical studies in developing countries

These studies in Central and Eastern Europe include: Claessens *et al.* (1997); Pohl *et al.* (1997); Weiss and Nikitin (1998); Frydman *et al.* (1999); Claessens and Djankov (1999); Frydman *et al.* (2000); Harper (2000) and Lizal *et al.* (2000) while the studies in Russia and the former Soviet Republics include both (Barberis *et al.*, 1996) and Black *et al.* (2000).

In addition to the studies cited above in this category there are several other empirical studies of privatisation in transition economies especially in Russia and the former Soviet Republics. As examples: Earle (1998); Earle and Estrin (1998) and Djankov (1999).

As can be noticed, examining the impact of privatisation on company performance is more difficult in transition economics than in non-transition economies. This is mainly due to privatisation in these countries occurring only as

part of large economic reforms or wide changes. Consequently, isolating the impacts of privatisation can prove to be difficult. Further, the data from transition economies is much worse and much more difficult to obtain than from non-transitional economies.

Furthermore, these studies employ different methods of privatisation in divesting SOEs, including asset sales, voucher privatisation, spontaneous privatisation, share offering or a combination of these methods. Also, these studies resort to different methodologies and cover differing time periods during the 1990s. Moreover, all these empirical studies examine either directly or indirectly the effect of privatisation on the company's operating performance.

4. Empirical Studies comparing pre and post privatisation performance changes

The most relevant studies pertaining to this research effort include: Megginson et al. (1994); Boubakri and Cosset (1998); D'Souza and Megginson (1999); Boubakri and Cosset (1999); Verbrugge et al. (2000); D'Souza and Megginson (2000); Dewenter and Malatesta (2000); Harper (2001) and Bortolotti et al. (2002).

The above studies adopt the same methodology to test the similar variables that were employed by Megginson et al. (1994). By using this methodology these studies can test and compare the pre and post privatisation performance of large numbers of companies, from different industries, divested in different countries and over different time periods.

12. LESSONS DRAWN FROM PRIVATISATION

There are many lessons that can be drawn from privatisation. Some of the incorporate points that have been made by researchers such as Liebreman (1993) and Havrylyshyn and McGettigan (1999) are provided below.

- 1- Private companies almost invariably outperform state run enterprises. In other words, any privatisation is better than none, no matter whether a stable, competitive environment has been established first or not.
- 2- Privatisation is a densely political process and includes denotative social engineering, especially in developing countries. Hence, without a well-defined political mandate and leadership from the top it is very difficult for a privatisation programme to proceed.
- 3- Private enterprises started from scratch rank as the best performers followed by newly privatised companies run by outsiders, either local or foreign. Privatised companies run by insiders are less efficient and productive, but even these regularly do better than state owned enterprises (SOEs). Researchers have not yet sketched the entire conclusion of the decisive role of start-up companies. But these companies' vigour and their contributions to economic growth, in addition to embracing competitive systems, trigger new issues that might affect the future of reform efforts.
- 4- Governments still want to restructure before privatisation in order to maximise value and avoid write-offs. The preferred way is to privatise as quickly as possible. The resources are generally not adequate to restructure. Nevertheless, large transactions will most likely need defensive restructuring efforts such as the writing off of unused assets, financial engineering and shedding of excess labour.
- 5- Economic reform, including establishing conditions for a stable macro-economic environment, financial sector reform, trade liberalisation, price liberalisation, abolishing of subsidies, a pro-competition policy and regulatory reform may be essential components in a successful privatisation programme.
- 6- A great number of the developing countries have now spent many years on the learning curve, mainly undertaking small and medium size transactions. However, these countries now are facing major privatisations with international implications, hence, they will certainly need significant external expertise in terms of investment banks, consulting institutions and environmental experts.
- 7- Since privatisation will take several years to complete especially in developing countries, corporate governance of SOEs and SOEs reform are still vital issues. Governments, however, have generally neglected such issues in

favour of endeavouring to accelerate the privatisation process. Despite this fact being understandable, they run the risks of creating a management vacuum and exposing many of their SOEs to go into bankruptcy. Hence, corporatisation or commercialisation are necessary preconditions for privatisation. They should not be viewed as privatisation itself.

13. CONCLUSIONS AND FUTURE RESEARCH

The review of the literature reveals that, privatisation had taken its first and biggest hold in the UK. It has however spread very rapidly throughout the world, affecting poor countries as well as rich ones, backward economies and advanced ones. It has been applied by both communist and capitalist governments and by democracies and dictatorships. Its universal applicability can be judged by its ubiquity. It affects countries in the East and the West, in the Northern and Southern Hemispheres, and has touched every continent.

Privatisation objectives are broadly similar across countries in that they concentrate on achieving benefits from re-balancing the roles of the private and public sector to enhance the productive power of the economy. Therefore, the major objective of privatisation is to develop the private sector and introduce regulatory reform in the public sector in order to improve efficiency, generate revenue or profits, create employment opportunities, improve the quality of services and develop capital markets.

There is strong evidence that privatisation is associated with improvement in the operating and financial performance of privatised companies throughout the world. Many studies provide strong support for this proposition, and perhaps only [Martin and Parker \(1995\)](#) and [Harper \(2001\)](#) report a decline in performance after privatisation (for 6 of the 11 British companies studied and for 178 Czech companies respectively). However, almost all of the studies that compare pre and post privatisation performance by testing changes in profitability, output, efficiency, capital investment spending and leverage, document significant increases in profitability, output, efficiency, capital investment spending and significant decreases in leverage.

The impact of privatisation on employment levels in privatised companies is still ambiguous. Some studies document significant increases in employment levels after privatisation such as [Galal *et al.* \(1994\)](#); [Megginson *et al.* \(1994\)](#) and [Boubakri and Cosset \(1998\)](#). Other studies document insignificant changes in employment levels after privatisation such as [Macquieira and Zurita \(1996\)](#) and [D'Souza and Megginson \(2000\)](#). A third set of studies document a significant decline in employment levels after privatisation such as [D'Souza and Megginson \(1999\)](#) and [Laurin and Bozec \(2000\)](#).

The conclusion therefore is that more studies of the impact of privatisation on the financial and operating performance of privatised companies in developing countries are needed. In addition, such studies should compare post privatisation performance with performance during a similar period prior to privatisation. Hence, a natural follow-on question is whether the above results hold for the privatisation programmes in some countries. .

A useful starting point for future research would be a study that comprehensively investigates the sources of performance improvement following privatisation. Such a study would attempt to ascertain whether performance improvement in privatised companies is related to real efficiency improvement or to exploitation of market power? (e.g. are profitability gains due to greater output and productivity, rather than to output price increases? and do efficiency gains result from better incentives and cost controls, rather than from wholesale firing of employees?)

It is also important that future research should attempt to investigate the relationship between the privatisation process and corporate governance, (i.e. the set of rules and incentives by which the management of a company is directed and controlled), as it is expected that corporate governance issues would vary according to the method of privatisation adopted. Future research may also attempt to examine whether privatised companies can benefit from more modern corporate governance practices and/or are certain ownership structures better for performance than others? Moreover, do all boards have the same effectiveness in practising control over managers in privatised companies?

Future research could also be directed towards comparing the managerial impact of privatisation as a main tool of reform with the impact of other approaches of reform (such as reinvention, reorganisation and reengineering). It is expected that those different approaches to reform could lead to different managerial impacts on the national, state and local levels in terms of: improved performance, increased efficiency and effectiveness, etc.

This study also reported that it is employees who suffer most in the privatisation process. Therefore, future research could also be undertaken to examine in an in-depth way the social impact of the privatisation programme. In particular, how privatisation affects human beings? Another consideration would be the appropriate approaches to overcome any weaknesses or disadvantages resulting from the privatisation programme.

Furthermore, analysis of the privatisation process by the National Audit Office and the Public Accounts Committee in the UK have revealed some issues regarding the underbracing of privatisation IPOs and has monitored the development by government over time of procedures carried out in order to tackle this issue (Hodges and Wright, 1995; Wright, 1999). Likewise, similar issues also result in respect of emerging economies, yet it is not explained the extent to which they are either recognised or are being addressed (Valentiny *et al.*, 1992). Thus, future research might focus on examining the development of the privatisation process in different developed or developing countries. Different approaches utilised by countries provide scope for comparative research.

Finally, comparative research that covers the impact of privatisation on financial and operating performance in different developing countries is needed. In particular, in the Middle East region and North Africa, as this part of the world seems to be much neglected in terms of research (Abdeldayem and Sedeek, 2018). These countries have also embarked on the road of privatisation and a study, which compares this, would be extremely useful and would shed important light on the impact of privatisation on financial and operating performance.

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