Does the Nature of Ownership Matter?
Lessons from Theory and Evidence

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Abstract: The primary intention of this paper is to seek whether or not ownership matters. By reviewing the literature, I would like to answer such questions as, what drives differences between private and public firms? Do those differences imply advantages that should make citizens prefer one type of ownership to another? Does privatization provide significant productivity improvement? Both theoretical and empirical evidences confirm that the nature of ownership is important. Changes in managerial incentives and enterprise objectives are likely to affect the performance of enterprises, like macroeconomic conditions, and/or technological developments.

Key words: State ownership, state owned enterprises, privatization and firm behavior

1. Introduction

In recent decades, there have been a number of policy reversals in the role of the state, especially with regard to ownership, in both developed and developing countries. Privatization has become an important tool for defining and redefining the role of the state in economy. A primary objective of privatization has been to increase the performance of state owned enterprises (SOEs). The term “privatization” was literally created by the Thatcher government who came to power in 1979 in the UK. Since then it has been accepted as a legitimate tool of statecraft by both industrialized and developing countries. Policy makers have publicly committed to the principle of a more limited role for the government in the economy. Since the mid-1980s, both developed and developing states have engaged in ambitious privatization programs. As a consequence, students of economics, management science, and public administration all have focused on the assessment of the performance of SOEs, and

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in the identification of the likely determinants of performance variation as a result of privatization.

Since Adam Smith, there has been a strong consensus that the freedom to engage in production, competition, free exchange, and property rights are central ingredients for economic progress. Cultural norms and institutions are often believed to explain cross-country differences in economic performance (de Haan and Sturm, 2000). Societies have limited resources, so they should decide on the best institutions not only to use those resources but also to distribute them among citizens and between current and future generations (Chamberlin and Jackson, 1987). North (1992) argues that institutions and their evaluation shape long run economic performances. According to North, societies should have a system that eliminates failed political and economic organizations. All these arguments imply that organization or reorganization of the institutional structure of the nation through privatization policies should receive considerable attention.

Furthermore, both theoretical and empirical literatures are likely to have policy suggestions particularly for developing countries. The public sector accounts for a substantial amount of employment and capital in many developing nations. Privatization is still underway in most of those countries. If state owned enterprises are as efficient as their private counterparts operating in similar circumstances, then the effort being dedicated to privatization has no benefits. Understanding whether privately owned firms perform better than state owned firms sheds light on whether national progress can be pushed forward by privatization.

The rest of the study is as follows. Next part briefly reviews how policy changes have taken place in terms of ownership. Secondly, conceptual thoughts on how the ownership differentiation, including privatization, led to performance differential at enterprises will be discussed. Thirdly, some empirical studies, more recent and influential ones, will be revisited. Finally, concluding remarks will be provided.

2. Role of the State as an Owner of Productive Assets

A brief analysis of rationales behind the creation of SOEs may enhance our understanding of the policy reversals that we have been experiencing recently. Basically, SOEs arose for a mix of political, ideological and economic reasons. In the 17th and 18th century SOEs were launched and undertaken in order to create revenue for governments in European countries. Following the Great Depression, new rationales and objectives were defined for SOEs. Moreover, right after WW II, tax revenues became a primary source for the government. Then, we have witnessed major policy
changes in the context of the role of the state almost all over the world. Movement to autarkic and corporatist policies has occurred in developing countries, diffusion of socialism in Eastern European countries and the progressive growth of mixed economies in industrial countries. As a result of both national and international developments in mid 20th century, intellectuals increasingly believed that the market economy was getting progressively weaker. Toninelli (2000) claims that the rising support in favor of public production could be considered a result of the deep crises that stuck liberal capitalism between the two World wars.

In industrialized nations, state ownership was viewed as the remedy for market failures. Market failure theory claims that in some cases social externalities cause an invisible hand to mismanage the economic activity, e.g. natural monopoly, which in turn produces suboptimal result for the society. According to the market failure point of view, when market failures occur, private firms tend to produce less than a socially desirable level, or they do not produce at all. Hence, governments use SOEs as a policy instrument in order to cure market failures. This implies that more market failures mean more roles for the government.

In developing nations this justification was added with the argument that state-owned enterprises facilitate “economic development” and “independence”. It was believed that stronger government intervention in the form of state direct production could resolve not only market failure problems but also increase the speed of economic growth and the creation of new jobs. In this sense, state enterprises create kind of bandwagon effect for the rest of the economy. As a result, in many developing countries, in particular in low-income economies, government enterprises function in almost every corner of the national economy. For instance, governments operate a casino in Ghana, make cookies in Egypt, and produce matches in Mali (World Bank Policy Research Report, 1995).

Besides market failure and economic development concerns, ideology has some explanatory power for the motivation of SOE creation. After WW II, an impressive wave of nationalization began all over the world. There was also an ideological motivation behind such policy movement. It was not a surprise that the main waves of nationalization occurred when labor, socialist, and social democratic parties were in power. For instance, in the UK the public sector was enlarged during the labor party administrations of Clement Attlee (1945-1951). In France, when Pierra Mauray’s

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1According to the market failure argument, SOEs should operate only in a limited number of natural monopolies in developed countries. In fact, during the early 1980s, SOEs’ shares in manufacturing industry were between 10 and 25 percent in those nations.
Socialist government was in power, almost 53 percent of the corporate capital of the country was taken over by the state (Tonielli, 2000). As a result, since WW II, almost all countries have experienced growing public sectors. In developed countries, government expenditures comprise 40 percent or more of the gross national product. On the other hand, in the last two decades, we have witnessed a reassessment of the role of the government all over the world. Since the late 1970s, the fortune of the SOE has been in steady decline. Intensive privatization programs have led to the progressive erosion of the public sector all over the world. An ideological and political upheaval about the large size and more functioned governments reaffirmed with the Thatcher and Reagan governments of the early 1980s, increasingly legitimized the idea that the state had become too intrusive to the economy, spending too much, crowding out private investments, and distorting personal incentives. These new ideas included, in addition, the belief that the welfare state was rewarding dependency and idleness rather than encouraging work, breeding illegitimacy and destructive behavior rather than requiring welfare recipients to assume responsibility for their own decisions. Hence, excessive state control was beginning to be considered inappropriate. The need for reducing the government to a more proper size was inevitable. Accordingly, reformers, not only in the U.S. and the U.K., but also in most other countries wanted to redefine the scope of the state, to dislodge it from preponderant positions, and to confine it to clearly circumscribed boundaries. The primary tool for reaching these goals was privatization (Spulber, 1997).

The declining fortune of public enterprise might be explained primarily by its increasing economic, financial and managerial difficulties. These difficulties derive from the public and political nature of SOE activities. Private ownership is thus seen as the means of unlocking gains in productivity by stimulating productive efficiency, offering greater motivation for both managers and workers, and creating incentives to enter new markets and to exit from declining ones. Lately, international institutions, such as the World Bank and IMF, have spent tremendous efforts to persuade the governments of developing countries to privatize SOEs. The major reason is the increasing skepticism about the ability of SOEs to produce efficiently. It has been argued that lower performing SOEs have a destructive effect on the economy as well society.

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2 It is possible to argue that ideological base behind direct public production may not have been just socialism, but nationalism or any form of autarky. SOEs in some countries are conceived as instruments for achieving autarky and for forcing the economy and society toward their superior destiny.

3 SOEs were intended to generate social benefits. However, experiences demonstrate that SOEs have proved to be an ineffective means of fostering such benefits in many cases among different countries, particularly the poorest ones. For instance, “Turkiye’ Taskomuru Kurumu,” a state owned coal mining
During the 1960s and 1970s, developing countries used SOEs as a primary policy tool for stimulating economic development. However, in the early 1980s, many people in those countries started to believe that the lack of efficiencies in commercial activities carried by SOEs contributed to the deterioration of their national economies. By using three performance indicators, World Bank Policy Research Report (1995) provides evidence how SOEs dampen the prosperity level of citizens in many developing countries. They assert that SOEs impede the economic well being of the society through the aggregate impact of inefficient activity at the microeconomic level and the fiscal deficits created by those inefficiencies. Smith and Trebilcock (2001) argue that SOEs have played a much larger role in less developed economies than in developed ones. On the other hand, we do not have clear evidence about SOEs positive contribution to the prosperity of those countries. Indeed, it is quite possible to argue that large and inefficient SOE sectors are costing developing economies dearly, particularly if one takes into account the opportunity cost of resources absorbed by SOEs. Furthermore, SOEs contribute to economic-political crises rather than stimulating economic growth and improving prosperity. Smith and Trebilcock (2001) say that

“...empirical evidence on the economic performance of SOEs generally yields negative results and suggests that SOEs are a major tax on the economies of developing countries reflected in the large operating subsidies required to sustain them (pp.217).”

In the early 1980s, the ongoing problems of developing nations affirmed the necessity of diminishing the size, scope, and economic functions of the state. Shortly after the economic crises of the early 1980s, many developing nations started to launch economic programs built upon the belief that “the more limited the role of the state in the economy, the higher welfare of the nation”. Like industrial countries, transitions -redefinitions of the role of the state in the economy- are supposed to take place largely by shifting boundaries between public and private sectors by launching privatization programs.

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*company in Turkey, accumulated losses of about 6.4 billion US dollars between 1986 and 1990. Per worker losses in 1992 was approximately $12,000, six times the average national income. Furthermore, employees worked under very poor health and safety conditions. A miners' life expectancy (46) was eleven years below the national average (57) (World Bank Policy Research Report, 1995). Obviously, all these imply that both employees and the government might have been better off if the government had closed the mine and paid the workers to stay home.*

*Advocates of privatization claim that divestiture of public firms leads to significant improvements in economic performance. Furthermore, they emphasize that the new policy not only lessens the financial burden levied by SOEs, but also provides an opportunity to divert scarce funds to growth promising public spending, such as education and health. For instance, diverting SOE operating subsidies to education.*
The number of privatization transactions, consequently, has been growing all over the world. For instance, according to Shafik (1996), between 1988 and 1993, more than 2600 transactions have been made in 95 countries, produced 271 billion US dollars. Additionally, Table 1 provides some idea about transformations in the role of the state by showing changes in state owned enterprises’ share of the GDP.

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<th>1980</th>
<th>1997</th>
<th>Change</th>
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<td><strong>Low Income Countries</strong></td>
<td>15</td>
<td>3</td>
<td>12</td>
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<tr>
<td><strong>Lower Middle Income Countries</strong></td>
<td>11</td>
<td>5</td>
<td>6</td>
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<td><strong>Upper Middle Income Countries</strong></td>
<td>10.5</td>
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<td><strong>High Income Countries</strong></td>
<td>6</td>
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Source: Sheshinski and Lopez-Calva (1999)

It could be argued that all these developments imply a significant revision of the role of the state as an owner of productive assets. In other words, a dramatic reversal happened all over the world in terms of the state’s participation in business. Thus, during the last two decades, privatization has become one of the universal economic issues throughout the world, and interest in privatization has been growing daily.

3. Theoretical Perspectives on Ownership

Privatization has become one of the most significant economic phenomena of recent years. In fact, the deliberation over ownership did not just recently come out; indeed, it is an ancient issue and has long been a central concern of economists. The idea that “private ownership is superior to public ownership” dates back to Adam Smith. According to Smith, both the decrease in public borrowing requirements and the improvement in efficiency are to be expected when the ownership is transferred from the public to the private sphere. Thus, the ongoing debate over privatization is the most recent round in a long lasting consideration over the proper role of the state.

would increase government education expenditures by 50 percent in Mexico, 74 percent in Tanzania, 160 percent in Tunisia, and 550 percent in India (World Bank Policy Research Report, 1995).

Privatization is defined narrowly as the transfer of ownership from public to private. Stiglitz (1989), on the other hand, claims that privatization has acquired a broader meaning. According to him, new policy symbolizes not only releasing government intervention, but also a strong belief that the society’s well being will be maximized if economic decisions are left to the market. The process of privatization
We may argue that the original question is phrased differently these days. Instead of asking “Can publicly owned enterprises produce more efficiently than its private counterparts?” the old form was “What kinds of goods and services should be provided by governments?” It is noteworthy to mention that the debate mainly took place on the ground of capitalism versus socialism (or economic planning), particularly during the second quarter of the 20th century. In calculation debate, many brilliant scholars, like Hayek, Lange, Schumpeter, contributed to a great extent. Besides Hayek and his few colleagues’ solid opposition, many of the laissez-faire economists, such as Simons, accepted government ownership in non-competitive industries even if their ultimate goal was to achieve competitive prices. Hayek and his colleagues’ theoretical challenges on state ownership did not gain significant momentum until the 1970s (Shleifer 1998). During the 1970s, empirical literature emerged to test theoretical predictions made by Alchian (1965) that SOEs are less efficient than their private counterparts. Studies directly applying insights to SOEs and privatization began to appear in the late 1980s.

In the mid 20th century, many economists, favored government ownership. The failure of the private market has been presented as an economic rationale for several government intervention and public ownership (market failure argument). According to the market failure point of view, when market failures occur, private firms tend to produce less than a socially appropriate quantity, or they do not produce at all. Thus, it has been argued that government intervention is needed if externalities, natural monopolies, and public goods exist. Governments may use SOEs as a policy instrument in order to cure market failures and internalize social marginal costs. The perspective that governments should take regarding market failures, as well as curing them, to internalize social marginal costs has been called the “social view”.

This view assumes both that political markets work efficiently and government maximizes social welfare. When a welfare maximizing government exists (political markets work efficiently), politicians and bureaucrats will act as loyal agents of the public. In these circumstances, competition between politicians enables citizens to endorse those who most strongly represent their well being, rejecting those who do not. Political competition, thus, coerces politicians either to design their policies with the interests of the voters or to leave office. Such politicians may always seek to maximize social welfare.

increases reliance on society’s private institutions and reduces the government’s role in satisfying the needs of the people.
Meanwhile, in the literature, market failure limitations on market mechanisms are paralleled by organization failure limitations on government actions. Opposing perspectives on the “social view” has raised questions about the ability of government intervention to mend market failures. According to alternative perspectives, “government failures” are, too, very likely to appear. These perspectives imply that the argument that market failures legalize government intervention is no longer so widely trusted. Public ownership may not always be the best solution to market failure even with a welfare-maximizing government. Besides, lots of questions emerge about public ownership when we relax the assumption that governments always act in the public interest. Efficiency losses involved in public ownership might be non-negligible. Furthermore, in some cases, those losses might be higher than the gains that can be obtained by solving a market failure problem. Consequently, the existence of market failure does not necessarily mean that government intervention will improve performance.

In short, the controversy for the idea that public ownership is the best solution to market failure comes from the likelihood of the existence of a self-interested government. Theories of self-interested governments underline serious imperfections in political markets (Shleifer, 1998; and Shirley and Walsh, 2000). “Government failure” literature uses two major cases that challenge the welfare maximizing government framework, agency problem and self-interested politicians and bureaucrats.

Vickers and Yarrow (1988) address the principal agent problem between voters and politicians. Efficiency of political market requires that voters be well informed about the actions taken by politicians and the consequences of those actions. They noticed that, indeed, this relationship between politician and voters suffers from significant information asymmetries. They assert that elections are poor mechanisms for producing information on voter’s preferences. In particular, it is very hard, if not impossible, for elections to provide information on specific issues, like the performance of an SOE. Another fact is that since the benefits of government policy are widely dispersed in most cases, all those who benefit have the incentive to free ride on any effort to support the policy (Olson, 1965). In an election with many issues, the average voter will not invest in acquiring information about the performance of an SOE (Vickers and Yarrow, 1988). All these points imply that voters, as a principal, might have great difficulty aligning the interests of the politicians (agents) with their own. Furthermore, similar agency problem is likely to exist between politicians and bureaucrats. Since SOE managers’ personal objectives could be different from those of politicians, a conflict emerges between the two groups. Managers might have an incentive to use their control to serve their own purposes at the expense of
profitability and/or social welfare. Consequently, there is a hierarchy of control from voters to politicians to bureaucrats, and this hierarchy faces principal agent problems at multiple levels.

Contrary to a welfare-maximizing government argument, public choice perspective assumes that politicians and bureaucrats behave like rational actors who maximize their own utility. Thus, it is another fact that SOE managers and politicians do interact in ways that benefit themselves at the expense of social welfare. More specifically, in a world of limited information, politicians can use SOEs to meet political goals at the cost of inefficient SOE operations. Shirley and Walsh (2000) argue that the degree of such behavior determined by the size of imperfection in the political markets. When the political market becomes more heavily distorted, a politician can deviate easily and largely from social welfare maximization. Such interventions are usually defined as distortionary and inefficient.

Political interventions mostly take the form of excess employment, above-market wages, investment in projects that benefit politicians rather than consumers, and skewed pricing. Shleifer and Vishny (1994) cite several example cases of political interference that make it evident that politicians do not hesitate to use public enterprises to garner political support. Their model shows that bureaucrats create employment that is politically desirable and economically inefficient, while politicians reward managers by budget increases in return. It implies that public enterprises are frequently asked to arrange their productions according to political desires rather than economic considerations. Thus, in some circumstances, public enterprises might function to fulfill certain distributional objectives. For instance, politicians are concerned, in many cases, more about raising employment -creating new jobs- than having economic efficiency, particularly if workers or unions have a significant influence in the political arena. For instance, the British government refused to close grossly inefficient coal mines to preserve mining jobs (Donahue, 1989). Ertuna (1998) displays that Turkish governments behave the same way. Similarly, Alesina, Danninger, and Rostagno (1999) show that the Italian government uses public employment as a kind of subsidy from the wealthy North to support the impoverished South. According to them, about the half of the wage bill in the South of Italy can be taken into subsidy circumstances.

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6 Frydman et al. (1998) show that politicization prevents SOEs from restructuring.
7 Donahue (1989) shows that publicly provided services employ higher workers per unit of output; thus, operating costs of public enterprises are higher than at private enterprises.
8 According to Ertuna (1998), Türkiye Komür İşletmeleri (one of the Turkish SOE-a coal company) employed 32,000 people as of 1994, while the optimal number suggested by feasibility studies was 12,500.
Boycko, Shleifer, Vishny (1996) extends the Shleifer and Vishny (1994)’s analysis. Boycko et al. (1996) stress that political intervention in SOEs is likely, since politicians receive all of the benefits of such interventions, but bear little of the direct (subsidies) and/or indirect (inefficiencies) costs. They also assert that it is more difficult, particularly because of more transparency, for politicians to subsidize private firms than SOEs to serve their political goals. A similar argument was previously raised by Sappington and Stiglitz (1987) and Shapiro and Willing (1990). Both studies asserted that state ownership reduces the cost of state intervention. Jones (1985) also investigates the use of SOEs by politicians to transfer wealth from one group to another. Jones (1985) finds that political transfer through SOEs are far more attractive for politicians, since such a way of redistribution is far less transparent than traditional taxes and subsidies.

As a result, agency problem and self interested politicians and bureaucrats arguments critically challenge the assumption of efficient market. Shepsle and Weingast (1984) claim that government intervention is not always the best response to market failure because of imperfect political markets. All these suggest that SOEs are the superior solution to market failures only in a relatively rare set of circumstances. Alternative perspectives to the market failure argument strongly assert that politicians and bureaucrats do not behave in the way that welfare maximizing government presume; rather, they behave as rational players who maximize their own welfare. Thus, SOEs will be used to serve the purposes of politicians in most political markets, at the expense of efficiency.

The crucial and old-fashioned question is “which ownership is more efficient, private or public?” Sheshinski and Lopez-Calva (1999) claim that the important point is how differently the decision process of the firm is affected by government intervention under either kind of ownership. According to them, this could be done by looking at how the objective and constraints are affected as a result of ownership change. Additionally, Shapiro and Willig (1990) underline the importance of informational and incentive differences between SOEs and private firms. According to them, those distinctions create varieties over an enterprise’s operating decisions and economic performance, which in turn determines which one performs better than the other. Sappington and Stiglitz (1987) raised a similar concept that the main difference between the two ways of production is the size of transaction costs that the government faces as a result of intervention.

Advocates of privatization assert that many productive activities taking place under the public sector can be carried out more efficiently under the private sector, since managers and workers have better incentives under private ownership. Shapiro
and Willig (1990) argue for the benefits of privatization through the existence of “bad knowledge” after divestiture. According to them, privatization yields bad knowledge for policymakers by constructing an informational barrier between policymaker and firm that prevents the self-interested politicians and/or bureaucrats from pursuing their personal objectives. Bos (1991) claim that divestiture promises a new organizational structure in which managers face better informed principal which in turn makes the principal agent problem less likely. Additionally, public firms face softer budget constraints since governments do not led them to bankruptcy. According to Schmidt (1996), time inconsistency of governments is the leading factor behind the soft budget problem. He asserts that if governments convincingly commit to not subsidize, and if they keep the promise credibly, firms produce more efficiently. Since privatization hardens the budget constraint firm managers face by cutting government supports and even making liquidation possible, productive efficiency definitely rises (Schmidt, 1996; Segal, 1998). On the other hand, Perotti (1995) asserts that privatization does not eliminate the possibility of political interference; indeed, it can only restrain government intervention over divested firms. He agrees that once a public firm is divested and privately owned, a politician’s capacity to interfere is reduced by the owner’s control on residual rights. It implies that government’s right to intervene is more limited under the private ownership. On the other hand, populist governments may put pressure over firms even after divesture by “arm’s length” policy tools (regulation, taxation, subsidies, etc.) in order to please voters and garner political support (Perotti, 1995).

Some researchers claim that intervention in private firms will also occur. They imply that problems of separation of ownership and control arise in both SOEs and private enterprises. So, there is no significant difference between public and private ownership in terms of the possibility of facing principal agent problems and political interference. For example, Chang and Singh (1997), and Vernon- Wortzel and Wortzel (1989) maintain that SOEs and large private firms must both contend with unwieldy bureaucracies; so, that private firms have no inherent advantage in corporate governance. Meanwhile, these arguments suggest that there is no guarantee that ownership transfer from public to private necessarily brings efficiency improvement.

According to conventional wisdom, in both types of ownership, agents seek to maximize their own utility rather than that of the principal. In private firms, this divergence is smaller than with SOEs, since the private market offers features, like ownership trading, the threat of bankruptcy, and the threat of losing jobs (or credibility), that can dampen it for private firms in many circumstances. Additionally, debt markets cannot play the role of disciplining the managers, because SOE’s debt
is public debt that is perceived and traded under different conditions. Since state-appointed managers do not own stock or stock options in firms under their control, and since the political market ensures that the peril of losing a job is less likely, they do not treat state resources in the same way that they would with their own property (Laffont and Tirole, 1991). On the other hand, under private ownership, managers realize that they will gain or lose as a result of their action. Managers, thus, have a strong incentive to behave responsibly.

4. Empirical Studies

Most of those studies have focused on the efficiency issue in order to address the question of whether ownership matters or not. Two hypothesis are generally tested: that the performance of privately owned firms are superior to that of state owned firms, and that the change of ownership in time from state to private (privatization) lead to improved performances. Because of the current stage of ownership debate, only papers which are interested with the second hypothesis will be considered in this part.

In order to compare SOEs with privately owned firms, we needed to find an appropriate set of comparison firms. Privatization has been a government policy tool for more than two decades throughout the world. Hence, it could be argued that the time period is sufficient for academia to carry out empirical studies of the effect of ownership change on the performance of former SOEs. On the other hand, data availability and consistency are still present as an important problem for testing the impact of ownership on performance. The possibility of sample selection bias is very likely to exist. Some opponents of privatization claim that most of the gains, if not all, documented by researchers after privatization resulted because of selection bias, rather than divestiture.

In spite of such problems numerous academic papers inspect the performance of private and public enterprises at many levels: a case study, at a single country and at international levels. Some of the existing empirical studies do provide weak support for the premise that privately owned firms are more efficient than publicly owned

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9 Selection bias can result from many causes, like the desire of governments to privatize the healthiest firms first to increase its credibility and/or to assure that they privatized successfully. Another sample selection problem, particularly for cross-sectional analysis, is that data availability tends to be greater in industrial countries. Mostly it is difficult to have such benchmarks in developing economies since most of them engage in limited private sectors. Hence, data from those developed countries might be over-weighted in the cross-sectional analysis. Furthermore, researchers should be careful when comparing accounting information generated at different times in many different countries especially for compromising emerging and developed markets.
firms. Contrary to earliest studies, recent literature has taken a much less flattering view of SOEs, and found results in favor of privatization. For instance, Galal et al., 1994; Meeginson et al., 1994; Ehrlich et al., 1994; Frydman et al., 1999; La Porta and Lopez-de Silanes 1999; D’Souza and Megginson 1999, all show that private ownership has a potential to increase productive efficiency and to improve the society’s welfare. In the following part, I will briefly discuss some of these empirical studies.

Ehrlich, Gallais-Hammonno, Liu, and Lutter (1994) empirically address the state versus private ownership by using data from a single multinational industry. By examining twenty-three airline companies from different countries between 1973-1983, Ehrlich et al. (1994) reached the result that companies under state ownership tend to have lower long-run productivity growth and/or cost declines. Their results show that, in the long run, complete divestiture would bring out 1.7 to 1.9 percent unit cost decline per year, and 1.6 to 2 percent productivity growth per year. However, their results do not suggest that significant change on productivity and costs in the short-run as a result of ownership changes from state to private. Hence, they state that the short run productivity level variation after privatization may not be so obvious. Furthermore, their results also suggest that a partial privatization contributes positively into long-run productivity growth; however, such contribution is much smaller than the benefits produced by complete privatization.

One of the most influential study in the privatization literature produced by Galal, Jones, Tandon, and Vogelsang (1994). Galal et al. (1994) has drawn substantial attention due to the methodology employed in study. The authors under took detailed case studies of twelve privatized large firms, mostly airlines and regulated utilities firms, from four different countries: UK, Chile, Mexico, and Malaysia. The methodology is counterfactual and makes projections of the firm performance under the privatized scenario and a hypothetical “public ownership scenario”. They compare the actual post privatization performance of the privatized firms with their predicted performance had they not been privatized. Comparisons between those two situations measure the changes in welfare. Welfare is measured through changes in total surplus, decomposed into several components. They found net welfare gains in 11 of 12 cases. They also found no cases where workers became worse off.

La Porta and Lopez-de Silanes (1999) provide evidences from a single nation but it is a multi industry study. La Porta and Lopez-de Silanes (1999) analyze the performance of 218 enterprises, privatized between 1983 and 1991, in 26 different sectors in Mexico, and find evidence that strongly support the private ownership. Even those firms were highly unprofitable before privatization they became very profitable thereafter. Output increased 54.3 percent, and sales per worker roughly dou-
bled, regardless of a reduction in investment spending and workforce. Their analysis addresses two criticisms usually made against privatization: (a) that the profitability of firms increase at the expense of society because of price increases, and (b) that the profitability comes at the expense of workers, whose labor contracts are less generous, involving significant layoffs. One of the most important features of their work is that the authors decompose the changes in profitability into price increases, labor reduction, and productivity gains. Their results show that profitability, measured by the ratio of operating income to sales, increased by 24 percentage points. Those gains are decomposed into the following components: (i) 10% is due to increase in prices, (ii) 33% comes from laid-off workers, and (iii) 57% was induced by productivity gains.

One of the most prominent works in the privatization literature is produced by Megginson, Nash and van Randenborgh. Megginson, et al. (1994) developed a proxy variable methodology to test whether a significant operational and financial performance changes exist between pre and post privatization period of divested firms. Their methodology is borrowed by more recent studies Baubakri and Cosset (1998), and D’Souza and Megginson (1999). Megginson et al. (1994) compare the pre- and post privatization financial and operating performance of 61 international companies that are fully or partially privatized between 1961 and 1990. Baubakri and Cosset (1998) test 79 international companies’ pre and post privatization financial and operating performances that are either completely or partially divested between 1980 and 1992. Similarly, D’Souza and Megginson (1999) evaluate pre and post privatization performances of 85 companies privatized between 1990 and 1996 through public offerings in different countries.

Taken as whole, these three studies provide evidences in favor of privatization by examining number of firms privatized through public offerings in different countries. The performance indicators analyzed in these three papers relate to mean and median levels of profitability, sales, operating efficiency, leverage, capital expenditures, and employment. More specifically, they provide empirical evidences that privatization bring out improvement in efficiency, profitability, output, capital spending, and leverage. However, there is no consistent result with regard to the employment. More specifically, contrary to D’Souza and Megginson (1999), Megginson, et al. (1994), and Baubakri and Cosset (1998) find out that such increments in financial and operating performances of divested firms took place without sacrificing employment.

Dewenter and Malatesta (2000) study the performance of 63 firms from both developed and developing countries, which were divested over the period of 1981-
Does The Nature of Ownership Matter? 15

1994. They examine the performance over two intervals; short-run interval -3 to -1 with +1 to +3 years, and long-term interval -10 to -1 with +1 to +5 years. Dewenter and Malatesta (2000) test three proxies, profitability, labor intensity, and debt levels. They show robust evidence that enterprises tend to have higher leverage and greater labor intensity when they publicly owned. In other words, their results confirm that leverage level and labor intensity decrease significantly after privatization over both the short and long run. On the other hand, they find mix results regarding profitability over the short and long run periods. Even though the study verifies some improvement in profitability, the evidence is not very robust.

Frydman, Gray, Hessel, and Rapaczynski (1999) compare the performance of privatized and state firms in the transition economies of Central Europe. Frydman et al. (1999) examine 218 survey data gathered from midsize manufacturing firms in the Czech Republic, Hungary, and Poland between 1990 to 1993. They compare the privatized group to the nonprivatized group with panel data through four measures of firm performance sales revenue, employment, labor productivity and costs per unit of revenue. Meanwhile, Frydman et al. (1999) explicitly try to eliminate selection bias by considering for potential pre-privatization differences between the two groups. Frydman et al. (1999) find that, on average, privatized firms perform better than the state owned firms; but such performance improvement is not automatic, at least for the transition economies of Central Europe. Furthermore, they emphasize that the size of performance improvement depends on the types of owners to whom divestiture gives control. According to their results, privatization produces significant performance improvement if the SOE is sold to outsider-owners, but not insiders.

Claessens and Djankov (2002) study the privatization benefits in Eastern Europe in the period of 1992-1995 using a methodology similar to Frydman et al. (1999). Claessens and Djankov (2002) inspect performance changes of more than 6000 privatized and state owned manufacturing enterprises in seven Eastern European countries- Bulgaria, Check Republic, Hungary, Poland, Romania, Slovak Republic, and Slovenia. They compare performances through four measures of firm performance sales revenue, labor productivity and employment; and provide robust results by launching different econometric specifications, like fixed effects, cluster effects, random effects. Claessens and Djankov (2002) illustrate that privatization bring out significant performance increases if the time elapsed since privatization is 3 or more years. Firms privatized for less than 3 years cannot significantly outperform state owned counterparts; indeed, they perform very much same. Their results imply that the length of time passed since privatization makes a difference over the magnitude
of performance change. Thus, the more time elapsed since privatization, the greater the increase in firm performance.

Harper (2001) study privatized firms from a single Eastern European country, Czech Republic. Harper (2001) develops accounting measures to test the changes in efficiency and profitability of 178 divested firms. Interestingly, he finds that even with a significant reduction in the number of employees, the operational efficiency and profitability ratios decrease significantly after privatization. According to him, such inefficiencies result from structural factors, like old production techniques and pricing strategies as well as lack of efficient management.

Also there are papers which are essentially case studies of individually privatized firms. Those enterprises function in areas which are generally believed to stay in government hands for political if not for economic reasons. For instance, Ramamurti (1997) examines the impact of privatization on the Argentinean national freight and passenger railway system. He found amazingly significant improvement in labor productivity, 370 percent. On the other hand, privatization brought out a substantial reduction in employment, 78.7 percent. Ramamurti (1997) also showed that consumers benefited from better quality services and lower prices. He asserts that such performance improvements could not have been achieved without privatization.

5. Conclusion

As recently as three decades ago, despite leaving commercial activities to the private sector, most developing countries saw the state as the engine of economic development. However, for the past twenty years, we have witnessed a reassessment of the role of the government. In this sense, the political and economic policy of privatization has been embraced around the world. Privatization reignited interest in the fundamental question about the role of government in the economy.

The failure of the private market has been presented as an economic rationale for several government intervention and public ownership. Meanwhile, in the literature, market failures are paralleled by government failures. The latter implies that the argument that market failures always justify government intervention is no longer widely believed. The market failure argument assumes a welfare maximizing government. However, information and contracting problems, for example, could create inefficiencies under public ownership. The political market seems far from perfect which violates the welfare maximizing government assumption. Conflicts that are very much likely to exist between principal (policy maker) and agents (bureaucrats)
would possibly be the source of a non-negligible size of inefficiency within the public ownership.

Managers (the agent) in both types of firms are assumed to seek the maximization of their own utility rather than that of the organization or its owners (the principal). However, according to general wisdom, there are important differences between public and private governance, and that those differences impact enterprise performance significantly. Private market has some features that reduce conflicts likely to exist between principal and agent. More specifically, in private firms, divergence between principal and agent interests is reduced through monitoring the threat of bankruptcy and the threat of takeover.

Empirical studies mostly suggest that SOEs function less efficiently than their private counterparts, particularly in industrial nations. In terms of privatization, privatized firms utilize their resources more efficiently and perform better than in the past. At the same time, someone could argue that privatization provides less promising results for developing countries. It is noteworthy to mention that those empirics usually focus on one rationale of privatization. In general, there are four major objectives in the privatization process: (1) achieving an efficient use of resources, (2) minimizing state involvements to create a better legal and structural environment for private enterprise, (3) raising revenue for public account and improving the public sector health, and (4) expanding and deepening the existing capital market. Another fact is that some of these objectives might conflict with each other. For instance, increasing the efficiency of production may not be compatible with the objective of maximizing proceeds coming from divested firms. Moreover, a successful privatization requires some further elements, such as a healthy private sector, sufficient capital market, effective regulatory structure, and minimized corruption that are not available in many developing countries.

Consequently, both theoretical and empirical evidences confirm that the nature of ownership is important. Private ownership can improve the performance of public enterprises. If such an efficiency improvement is likely in all sectors, then large gains in terms of efficiency could be obtained by further privatization of the economies.

Özet: Bu çalışmanın amacı, mülkiyet farklılığının (kamu veya özel) ekonomik anlamda önemli olup olmadığını araştırmaktır. Başka bir ifadeyle, teorik ve ampirik literatür gözden geçirilerek “kamu ve özel firmalar arasında verimlilik açısından farklılığı sebebiyet veren faktörler nelerdir? Bu farklılıklar, ülke vatandaşlarının mülkiyet türlü üzerinde özel bir tercihe bulunmalarını gerektirir mi? Özelleştirme firmaların ve-
rimliliğinde anlamli bir artış yaratır mı?” gibi sorulara cevap aranmaktadır. Teorik ve ampirik literatür üzerinde yapılan analiz, mülkiyetin önemli bir unsur olduğunu sonucu verebilmektedir. Özel mülkiyetle birlikte, gerek yöneticilerin motivasyonlarındaki değişme gerekse mülkiyet sahiplerinin amaçlarındaki değişme bir teknolojik yenilik gibi firmaların performansını etkileyebilmektedir.

Anahtar kelimeler: kamu mülkiyeti, kamu firmaları, özelleştirme, firma davranışları

Reference


