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Privitization meanings, methods and cases- a short note

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Abstract: Privitization is one of the cornerstone projects of the countries seeking to speed up their economic growth. It is the project of prioterizing the market mechanism by returning to it the functions unduly overtaken by the forces of the state. In more realistic terms, the domain of privitization may extend from total ceeding the ownership of publicly owned and opperated enterprises to the private sector at the one end of the spectrum to restructuring of government owned and opperated enterprises based on comercial principles at the other end. Therec are however certain prerequisite that need to be met before privitization can work effectively that for the most part amount to provision of an environment that is conducive to large scale and effective private sector engagement in economic activities. Contries that are more successful in providing this environmrnt are in a superior position to rip the advantages of privitizatios. A first task in the the study of privitization in varuis contries , therfore, is to study how suceessful they are in providing an environment conducve to privte sector opperatoions. This paper's focuss is on privitization in Iran; It includes an analysis of privitizations from the stand point of both the required environment including the institutional requirements and also of policies. The experience of privitizations in certain other countrires is reviewd in order to give the analysis a comparative perspective.

Key words: privitization preconditions, privitization policies, Iran's economy

1. Intoduction.

Privitization of government companies has become a world wide phenomenon. First, developed, and then devoping countries have embarked on ceeding a diverse range of government owned enterprises. The international lending institutions such as the World Bank and the International Monetary Fund are said to have set privitization as a pre-condition for approval of loan and other types of finnacial assitance requests.

The process of privitization is sometimes slowed down due to the reluctance of government officials who find it hard to let go of the companies under their jurisdiction. On the other hand, even though government dis-involvment in the economy may yield positive outcomes at the comercial level, its simultanious impact at the social level may not always be positive and as desirable. Hence, countries embarking on privitization need to mitigate, or eliminate altogether, the negative social outvcomes of privitization through measures and practices such as deregulation and good governance Boubraki,(1998)

Privitization in different countries is carefully timed to mach country specific condition and economic environment. Iran also needs to time its privitizations in accordance with its own specific conditions and economic environment. Iran also needs to take initiarives to provide for the tranquility, stability and security pre-conditions usally required for motivating long term private sector investment in the economy that facilitate provitizations

kikeri, (1994)

On the otherr hand, Iran's prospects for further integration into the world economy, especially the WTO structure can be enhaced possibly by giving some initial support to the private sector through adopting the needed supporting rules, regulations and policies that lay the ground for more extensive presense of the private sector in the economy with the private sector feeling a real sense of competition with lessr government role as an owner and manager of enterprises.

Having said that, one could argue that due to the strutural problemd prevalent in the Iranian economy, the process of privitization has suffered from certain impedients that include among others, certain ambiguities and non-transparencies in the laws and regulations governing privitization. On the other hand, given the still hirearchial structure of the Iranian soceity, and a public who still views the government as its a guardian, policy makers have opted to exercise certain expediency in privitizations in order not to disappoint the public opinion. So as one analyst observes in spite of the fact that privitization has been a main agenda of the Iranian government over the last two decades or so there still is widespread incidences of a heavy presense of government owned companies in the economy and also of an increase in government or government dependent employment under various pretexts

Torkeman (2003)

This paper is intended to collaborate on privitization both conceptually including the reqired preconditions and also empirically as the case is unravelling in Iran. The experience of some other countries als are reviewed in order to put the Iranain case in a comparative perspective. Section 2 that follows this introductory section is a conceptual treat ment of privitization including its pre-requisites. Section 3, gives a brief historical introduction and presents privitizations as implementd in England and Turky.Section . Section 4 focusses on Iran and 5 summerise and conclude the paper.

2. Meanings and Pre-conditions

2.1.Meanings

Privitization in simple terms is ceding government owned industries and enterprises to the private sector; it is a process of relinquishing government companies and establishments for aqusition by the private sector. Privitization in in international jargon is sometimes understood as delagation of responsibility for the economic affairs to the people. Privitisation in more general terms is a culture through which the government and all its decision making bodies will reach the belief that in reality what is of conern to people must be ceded to people because people can manage their own affairs better than the government can do it for them. In other words, the government should cede to people those affairs that people can operate better than the government. According to this understanding, privitization in all arenas especially in the economic arena, can provide a ground for more active participation of people in social, political, cultural and economic affairs and undoubtedly this wide participation of people in a soceity can strengthen the pillars of democracy with an enhaced role for people to increase their supervision over the government's operatins particualry government's economic opperations.

Privitization can encampus many different actions. The immidiate action as the term privitization connotes, is ceding the ownership and control of activities to the private sector perhaps via selling shares. Another is a reduction in government interference in the economy altogether including elimination of subsidies, deregulation or any combination of these thereof.

In the terminology of Adams(1996), privitization means any action that targets the expansion of the domain of the the activities of the private sector. It is a process through which the government studies the feasibility of transfering to the private sector of its functions and establishments at all levels and if waranted performs the actual trasfer.. Beeslyand, Little Child(1983) see privitization as a means for improving economic activities through the role playd by the market subject to the requirement that at least 50% of shares in any venture is held by the private sector. Veljanovski(1987) considers privitization as private sector undertaking of economic activities while asset ownership is transferred to the private sector.

During the first session held by the Asian Productivity Organization in Indonesia in 1993 under the banner of coordination privitization in member countries, privitation was refered to as denationalization, deregulation and liberalizations with total transfere of legal control over firms with implications for retuning to the private sector of nationalised entities, removal of all barries interfering with the prevalence of perfectitly competitive market conditions in the production units. So in general terms, it can be said that privitization is a process that celeberates the rebith of commitment to the belief that markets are more efficient than government and that the Smithian Invisible Hand knows best. It makes questionable the the efficacy of government activities and requires the the public sector (the government) to limit its activities and cede to the private sector the ownership or the management of some of the entities under its ownership and control.

2.2. Preconditions

The basic objective of privitization is to change the role of government in the economy from opertional to policy making and monitoing activities and cede to the non- government sector operations such as industrial, production and service activities (Bell, 1995).

There are two preconditions for any sucessful privitizations:

a) oppenness of the trade regime in the country concerned and existence of an appropriate and secure environment for investments that meet the soundnss and developmental requirements which motivate developed capital markets and competitive comodity and service markets(Kikeri, 1994).

b) the ability of the market to absorb the labour released in the process of privitization(Adams, 1992).

After setting objectives and meeting the pre-conditions, attention should is turned to two important priciples of profitability and reinforcement of private ownership. A review of privitization in countries such as Germany, Britain, France, Russia, South Korea, Check Republic, and Slovakia that differ in some fundamental ways in their economic, social, cultural and behavourial set up reveals that this two principles have been adopted in the transition from a public dominated economy to a market dominated economy and relative to their time, space and situation have provided for the following grounds:

1) taking managerial measures internal to the firm with the purpose of increasing firm's productivity. These include measures such as shaping the correct attitude among emploees and managers, development of human resources, putting into efffect better financial management practises and practises that increase the productivity of capital, restructuringengineering with the purpose of reducing the managerial and administrative hirarchy levels, integrating homogenious activities , eliminating parallel activities, development of the internatioinal affairs for facilitating capital and technology inflow, revising contracts with the purpose of increasing transparency and also defining and offering standars and private contract provisions.

2) Creation by government of an environment that acts as the engine of privitization.

This paper argues for the deficiency of these elements in the context of the Iranian privitizations. It is apparent from even a cursory examination of the laws, development plans and privitization proceedings that the government falls short of having a comprehensive, well-coordinated(particulary among institutions and organizations) and complementary package set that reflects on the strategy and objectives of privitizations in Iran.

3. Actual Cases of Privitization .

3.1. A historical overview.

During the perid after the first world war(1914-1918) with the socialism of the Ex -Soviet Union (1917) in place, government interference in conomic affairs was at a peak. Notable economic achievements were made by expansion of demand and public and welfare servises , reduction of unemployment and mobilzation of economic potentials. The public ownership domain was expanded and many industries and economic activities in European countries were nationalized. The nationalised enterprise included: many investment banks and bank affiliated inductries in Italy, banks, coal industries, railways, airlines and gas in England, and insurance institiitions, banks, weapon manufacturing, and airplane manufacturing in France. Hence during the post war period, Europeans experienced extensively with managing government companies and national monolpolies. But at the end, the governments failed to controll for efficieny in nationalised industries and there grow an awareness for the need to change direction from nationalization to de-nationalization.

In late 1970's dischantments with governments grew mainly due to governments folowing confusing objectives, reduced work incentives, bureacratic pressure, growth of watsefull monopolies and mnagerial weakness. This gave rise to the idea of calling an end to government involvement in the economy, a sort of political liberalism, associated with market friendly economic policies.

The thoretical underpinings of the industrial revolution of the second half of the eighteen century and the idea that government interference in the economy was best minimalised and limited to certain special spheres while leaving economic afairs to the workings of free markets based on Adam Smith well known thesis were used to feed the new movement towards market economy.

Privitization was recommended globally as a strategic alternative to state ownership and control of the economy. England became a pioneer in privitizations followed by many other countries in the world. The World Bank and International Monetary fund intitiatves to make their loan and financial assitance programs contingent upon privitization as recommeded by their staff provided aditional incentives for the countries to privatize. Models of 1950's through early 1970's had to be rewriten to reflect the new drive for privitizatin. The sucessful models suggested for 1980's and 1990's were models that depended upon private markets.

The group of small and medium size firms that did not operate profitably due to financial mis-management could be privitized by means of negotiation and/or biding. In england, when Margaret Tacher reached power, about 5.11 percent of the Gross National Product belonged to government companies. When she won re-election for the third in 1987, this share was 5.7 percent and during this period, more than 500 thousand labourers were relocated in the private sector and 90 percent of them became factoory shareholders.

An OECD report shows that in 1966 the member country governments earned $billion 88 from privitizations. In the meantime privitization spread to developing and OECD non- member countries, but the share of these countries in total privitizations were only 17 percent or $billion 4 in 1990.
Given the world wide derive for implementing liberalizaion and privitization policies and given the fact that government enterprise in Iran often opperate at eficiency losses, the Iranian privitizations and transfering certain government affairs to the private sector the Iranian law and policy makers came to belive in privitizations as a practical solution for improving the profitability of the Iranian firms(www.ipo.ir)

3.2. The Case of England.

The beginning of privitization in England goes back to 1979. England is one of the countries to start privizations without there being any prior experience with privitization anywhere.
The hisstory of England is a witness that up to the year 1979, the government involvement in the economy was extensive. During the ninteen century, numerous enterprises were put under the government custody. In the twentieth century, certain market failures, the Great Depression, the second world war, and the influence of labor parties lead to the expansion of the role of the government in the economy of England. The justification offered by the ruling power was rationalization of resource allocation and increase in efficiency.

When too much government control of the economy precipitated an economic crisis, the conservative seized the opportunity to take political power in its own hands. The party, lead by Margaret Tatcher, then, made privitization as its main agenda. The main privitization methods geared to government desired objectives in England included: sales of common stocks, direct sales, ceding to the managers and employees and finally sale of assets to the private sector.
To facilitate the progress of privitization policies, the British government implemented certain reforms during and after privitizations. These reforms included improving the financial position of the firms, removing the non-economic objectives governing the firms and putting emphasis on commercail and economic objectives, relocating the labour released as a result privitizations, devising the needed rules and regulations at each stage, exercising trasparancy in publec anouncements and information dessimination and total political commitment and concensuss building among political authorities and factions.

England began privitizations with ceding of smaill industries and non- essential services. To reduce the government size, it decided to cede public monopolies to the private sector that included ceding companies in communication , gas, airlinem industry, and vehicle manufacturing. The British steel company, shipbuilding, railways, transportation companies were cedded directly to the managers and employess of these companies. The British govermnent's main concern was to distribute the ceded shares to as manty people in the soceity as possible in order to encourage wider participation and responsibility in maintaing the ceded asssts.
and that is why the government offered to sell shares at low prices as an additional incentives to ecourage a wider polpulation to buy shares.Bonuses(prizes) were offered to shareholders who held on to their shares for longer periods of time. The london stock market acted as the medium where shares of large companies were offered for sale.

Privitizations in England were rather quick to achieve their objectives. The number of shareholders reached 12 million persons and revenue obtaind from the ceding of large companies amountrd to $billions 58. The share of nationalized industries as a percentage of GNP was %11.5 in 1986 (Vickers(1988). Gains in efficiency were observed too. In short, it appears that privitizations in England are geered twoards long term goals even if they might nor bear drastic short term commercial results.

3.3. The Case of Turky.

The idea of privitization began to attract the attention of the political leaders of Turky since the middle of 1980's as a way of speedingg up Turkish industrialization. But Turkish authoriries faced formidable probblems: a limited stock market, lack of corporate accounting standards, unfamiliarity of the public with the exact operation of stock markets, prevalence of financing budget deficeits through selling government bonds and finally the rigidity of the managerial structure of government companies. But in spite of these problems, the government took the first steps of privitization in 1987 where it anounced ceeding of 22 government companies that included the largest electric appliance maufacturers and steel and other manufactures of industrial products folowed by privitization of other companies.

The year 1988 witnessed privitization of communication equipment and 1992 privitization of airline companies. The method of privitization was sales to the public through the stock market. A number of the companies offered for sale were bought by foreigners. Based on existing statistics, Privitizations in Turky have lead to faster economic growth(www.ceri.ir; IMF 2000).

3.4. The Case of Iran

Privitizations in Iran were first outlined in 1989 by the policies of the 3rd Five Year Development Plan and decrees for implementations were issued in 1991 by the board of Ministers. During the 1st and 2nd Five Year Development Plans, policies had been outlined in the form of Notes for improving the operation of government companies and a more active presense of private sector in the Iranian economy. Note 32 of the law of Development Plan, decrees isued by the Board of Ministers in 1991 and 1992, the law of the manner of ceding government shares to benevolents(war security related veterans)and workers, the law passed by the Islamic Consultative Assembly in August, 1994. Note 35 of the law of the country's budget for 1998 and 1999 are among the initiatives taken to prepare the grounds for privitizations according to the dictates of 3rd Development Plan. The program of privitization, then, proceeded according to the dictates of the 3rd Development Plan. In the second and third chapter of the 3rd Development Plan Law, there are 23 articles that determine the manner of overhauling government companies and ceding shares belonging to the ministries, organizations, and government companies. The articles of these two chapters rule the shaping of relevant policy making and excutive bodies needed to overhaul the government companies and offer them for sale in the stock market.

Shares belonging to government between 1991 qnd 2001amounted to rials billions 8329. However, ceding of public enterprises to the private sector moved rather slowly in 2000 mainly because of the lack of transparency in pricing the shares of government enterprsies offered on the stock market. The method of privitization during these years included offering the shares of government establishments in Tehran stock exchange, selling shares to emploees and managers mainly through the Ex- organization of extended government ownership of production units and direct negotiations on sale of government units. However in 1998, the negotiation method was abandoned due to the lack of pricing transparency and occasionaly fraud. Among enterprises that were included in ceding were: the organization for expansion and renovation of the Industries of Iran, the organization of national Industries of Iran, the financial organization of the expansion of government ownership. Over the said time frame, the the privitization organization has ceded 127 million shares of production units to workers mainly throgh the stock market. Futhermore, in recent years based on

Note 10 of the country's budget law it was determined to tranfere the shres of the government companies to the retirement organizations as a repayment of government debt to this organization(Safarzadeh, 2002).

The policies of privitization in 4th Development Plan follow closley those of the 3rd and are a continuation of the same. The Article 6 of the law of the 4th Development Plan calls for privitizations in all cases including the cases that fall under the Article 44 of the constitution and the general policies of the plan with the aim of strengthening the non- governemnt sectors by an assortment of privitization methods including: de-regulation, ceding management(like signing general lease contracts , management contracts) and owenership(inclding lease ending in ownership, slae of part or all of the shares, ceding assets), braking enterprises into smaller entities siuted to ceding, disolving and integrating companies. But as the main campain of the curent government is centered on social justice, special attention is given to privitization rationing (justice shares) in order to prevent an income gap among the various segments of the population and make for a fairer ditrubution of ownership and income in Iran. The system of "share ratining" is meant to promote equity in ownership, achive economic devlopment accompanied by socail justice and optimize the government size. Share ratining, ralative to ther method of ceding, facilitates and speeds up the ceding of a larger nubmber of enterprises that lack attraction to private investors.The bylaw governing the distrubution of justice shares as passed by the vote of the board of ministers comes in 13 articles and the government in intent to cede the shares of public enterprises to the lower income quittile of the polulation with a 50 percent discount and collect the proceeds on a 10 year installment basis in the form of keeping the dividends accriung to these share. This will be done by investment companies and justice share cooperatives established in the center of each State and each Townnship reprectively, under the supervision of the privitization organization.
It shoud be noted, however, that during fifteen years of privitization only 3 percent of government companies have been ceded and expansion of government companies during this period has parralled the expansion of privitizations

The main impedients to privitizations in Iran are: an overvalued exchange rate volatility that discourages capital goods and intermediate goods and tecknology imports, the underdevelopmet of organized capital markets, unpredictability of government regulatory system, constraints imposed by the constitution, the labor law, the tax and commercial law, procedural deficiencies and gaps, multiplicity of decision making bodies and an secure economic environment that propels private sector activity.

In addition to what just was said, there is some concern among the public that privitizations might lead to GNP decline, unemployment, isolations from the government and welfare reductions. Perhaps this is because Iranians are not yet ready to trust the private sector as they a trust the government with all its defciencies.
Besides, privitizations have not yielded the desired results homogeniously accros various host contries. The outcome of privitizations in India ,for example, have not produced the same positive results as in Canada, Malasia, the Check Republic and Poland.

For the most part, governments tend to retain profitable enterprises and only financially bukrup conpanies are offered for privitizations that fail to generate an effective demand.

Public decision makers at lower levels also are concerned about their own job security and that is why they exercise extreme expediency in implementing privitizations.
So in all, it may be sai that unattended privitizations will not necessarily produce the desired outcomes in Iran. There is now enogh experience in the world that can help Iranian policy makers choose the privitization scheme and mix of government/ private sector cooperative sector and NGO's that best meets the Iranian long term economic objectives and also the public expectation of restrucuring the Iranian economy.

4. Summery conclusions.
To sumerize, privitizations have a wide ranging epistem. They can convey several interrelated concepts such as transfere of ownership to private sector- total or in part. It does not necessrily connote ignoring the plight of the workers, and social services the less advantaged. It does, however, bear strongly on eliminating ineffciencies, and wastes resulting from governments burdening the economy in the form of government ownership, management, control and interference in the working of the markets.
In Iran, the foundations for privitizations were laid by a revisit of Article 44 of the constitution that called for denationalizations in a manner that would encourage more participation of the private and cooperative sectors in the economy. The justise share method of privitizations is intended to promote equity in the distribution of shares. The Iranian authorities have acted rather cauciously in their privitization moves and this has slown down the process of privituzation. That, at least in part, is because the environment and the preconditions of privitizations are not yet built. It is also because, privitizations are politically sensitive and as the cases of the countries reviewed indicate, because of the nature of methods adopted in privitizations, one sometimes gets the impresion that privitizatios are not really provitizations per se.
In the specific Iranian case, it appears that the infant industry argument once poular in developing countries applies to the private secto as well. It cries for help in order to start walking and if this is the case what happens to the need for reducing the government role in the economy. Or perhaps Iran should move slowly until the private sector start walking by itself.

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