

# PRIVATIZATION WORLDWIDE

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PRIVATIZATION WORLDWIDE

Adam Smith Institute

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## PUBLIC AND PRIVATE SECTOR

Although there has long been statistical evidence to document the comparatively poor performance of public sector production, the development of a theoretical framework has emerged only recently. The inefficiency and low output of the nationalized industries in post-war Britain, for example, has been widely acknowledged, first in popular anecdote, and later in scholarly reports which compared their performance to private sector counterparts both in Britain and abroad.

Many ad hoc explanations were offered to account for this. It was first suggested that the second world war had destroyed their capital plant and equipment, making them labour under insuperable burdens of replacement. This provided a convenient explanation for their poor performance, but failed to deal with the cases for which it was visibly untrue. A later suggestion offered was that the nationalized industries laboured under the handicap of not having had their capital equipment destroyed by the second world war. It was suggested that the other European countries, by being forced to replace destroyed stock, had been able to modernize, leaving their British equivalents still using hopelessly dated equipment.

A further attempt at explanation suggested that it was only the failing industries which had been nationalized in the first place and that a poorer performance was only to be expected because of this. One harder to disprove suggested that the state sector in fact provided non-measurable benefits whose presence was ignored by mere statistical tabulation. Thus, public sector hospital cleaners might be less efficient and more costly than the private counterparts, but this was because they stopped to chat to the patients, and therefore provided a valuable part of therapeutic care.

It was many years after the comparatively poor performance of the public sector had been well documented that these co-incidental explanations gave way before the understanding that the public sector is inherently inferior in its ability to deliver goods and services. It is not the presence of accidental factors which accompany the public sector supply that undermine its efficiency, it is the fact of public operation itself.

The public sector is not exposed to the commercial pressures which generate efficient operation within the private sector. For example, a public operation which fails to satisfy its market does not risk bankruptcy in the same way that a private firm does. There is thus absent an important spur to efficiency.

A public sector operation is usually protected by a complete or partial monopoly, and thus misses the impetus which the presence of competition provides. A private firm must constantly watch to keep its costs down and keep its output attractive, or it risks a competitor taking its market. A public monopoly knows few such pressures.



Absent, too, in the public sector is the compulsion to innovate, to keep abreast of new technology, and to keep a watching brief on the newest cost-saving developments. Without rivals to take away its business, the public sector is insulated from these important pressures.

Its protected position enables those engaged in production to direct the production of its goods and services to the satisfaction of producer needs ahead of those of consumers. Since the customers have nowhere else to go, they are, in a sense, captives, and are denied the input pressure they gain when they are free to take their custom elsewhere. The public sector is thus vulnerable to producer-capture, and is characterized by the provision of services which take more account of the convenience of the producers than of the needs of consumers. It is in the public sector that "unsociable hours" are banned, and weekend rundown or closure is the norm.

A further effect of this is over-manning. Ultimately, in the absence of effective consumer pressure, it is easier for the administrators to meet the needs of the workforce. The monopoly gives it the power to shut down a service for which the public has no other choice.

A more subtle effect of producer capture in the public sector is the under-capitalization which results. This occurs because the finance is dependent upon what legislators think taxpayers will bear, given all of the competing demands on public money. In practice this tends to mean that finance is tight. Given the pull which the workforce is able to exert in the public sector, there is a constant tendency for funds to be over-directed toward the current side of the account, and at the expense of the capital side. The workforce can be assuaged by this, and the threat of damaging dispute averted. Thus comes about the notorious depletion of capital to which public sector operations are prone.

At the apex of all of the problems associated with public sector supply stands the status of the operation as a political entity rather than a commercial one. The public sector operations are directed by an administration ultimately responsible to the legislators. The decisions made cannot thus be commercial ones, but must respond to political pressures.

At the simplest level, the available finance, for example, is not a function of anticipated consumer demand, or of what can be attracted from investors making a commercial assessment. Instead it is based on what legislators think the public will bear. It thus depends on the nation's current economic health, and on the political pull which bears on the legislators.

The funds allocated to each operation do not depend upon any commercial viability, given public demand, but on the comparative skill of the administrators in fighting for greater allocation to be made in their direction. Political in-fighting thus commands more success than commercial judgement, and the provision of the



level of supply is determined by its outcome.

The status of public sector operations as political entities has effects right through their range of decisions and activities. Because they are nominally answerable to government, legislators stand to incur public hostility or gratitude, according to their actions with respect to them. Thus the decision whether to keep a particular service open, or whether to extend it, will often be made on the basis of political pressures felt by legislators, rather than on economic viability.

Even such detailed decisions as the price for particular goods and services, or the hours of operation, are subject to the intervention of legislators seeking political rewards. In a celebrated case in Britain, a state railway branch line was kept open despite utterly unacceptable costs because it passed through no less than four marginal parliamentary constituencies.

In several countries the public sector operations feel the need to assuage legislators more strongly than they feel any economic pressures. Jobs may be given in response to requests by powerful politicians, rather than on the basis of merit or of need for personnel. Even in Britain the spectacle is of several public sector operations retaining a very large public relations presence in proximity to parliament, calculating correctly that the pressures on them from the political world are more real than those from the commercial world.

With the recognition that public sector operations are political entities rather than simply economic ones, it comes as little surprise that they often fail to measure up to exacting economic standards. The theoretical framework outlined above helps to explain their poor performance when set alongside their private sector equivalents. It shows why the empirical evidence reveals them as more costly, less efficient and less responsive to consumer preferences. It explains why their equipment tends to be out-dated, and why they are slow to bring in new types of service and technology.

Their status as political entities helps to explain why they are chronically under-capitalized, and are prone to making decisions in response to the political needs of legislators, rather than to the inputs of consumer requirements.

It is ironic that the public sector operations were once conceived as a way of giving society better services at lower cost, and that it was thought at one stage that without the costs of advertising, profit or competition, they would out-perform the private sector. The reality has been the reverse of this. Without commercial pressures or the competitive stimulus, they have been less responsive and more expensive.

By turning to the public sector for the supply of goods and services, countries have handicapped their own economic performance. They have contrived a position in which they have



been paying more than necessary for these operations, and yet failing to gain services which responded to needs and moved with the times. This, in turn, has raised the input costs of their private sector industries. By paying more than they need for such things as communications and transport from the public sector, the costs of their other goods and services were increased.

A major problem encountered in the attempt to deal with the problems posed by public sector operations has been that their political status has to a large extent sheltered them. The built-in interest groups of the public sector have proved too large a hurdle for the political process to surmount, and have thwarted legislative attempts to redress their difficulties.

Attempts to curb their spending, for example, have encountered opposition from the administrative staffs which ran them, the workforce which manned them, and that part of the general public which benefitted from their activities. In view of this, the fourth group, the legislators, have not been able to pursue and sustain such campaigns.

Similarly, the attempts to eliminate unnecessary public sector activities have also seen little success. They are not perceived as unnecessary by their beneficiaries or by their own staffs. The public at large, as taxpayers, perceive too little drain of resources by each operation for it to motivate them in support of elimination.

The determination to cut out the wastage, at least, from public sector programmes has met with no better result. Although the intention might be to cut down on overheads and administrative duplication, in practice it is easier for the administration to cut into the service itself. When cuts are proposed in the most popular parts, the legislators soon feel public pressure to restrain their initial enthusiasm.

Even the modest attempt to bring in the efficient methods from the private sector fails to achieve results of any significance. The efficiency experts may come in from private companies, and may study and report new recommendations. Ultimately the changes which they proposed do not last. The public sector is not under the pressures which sustain efficiency in the private sector. The methods do not take naturally, and are at odds with the pressures felt in the public sector. The history of public supply is full of the reports of business experts and the determination to improve operating methods. It is far shorter on any successful outcome to such well-meant resolutions.

The public sector cannot be made to respond like the private sector of the economy because it is fundamentally a sector of the political world as well as the economic world. It is part of the political process and governed by political pressures. It cannot be made to share the advantages of the private economy because of this very fact. It is in the light of these findings that some attention turned away from the attempt to improve it, and toward



methods of actually transferring its operations into the private sector itself. This is the origin of privatization.

Privatization represents the determination to have done in the private sector a part of the activities which were hitherto performed in the public sector. It cuts the gordian knot, and manages to achieve the virtues of the private sector for public supply by actually moving it into the area where it is subject to those pressures.

In the process of privatizing public operations, many different methods have been tried, and many have been successful. Most of them involve creating for the interest groups concerned a greater advantage in the privatized concern than they enjoyed when it was in the public sector. Thus workers are allocated share issues, administrators are changed into company boards, and the public receive the benefit of choice and improved service offering, as well as the opportunity to invest. With the satisfaction of the interest groups comes the support of the fourth group, the legislators.

Privatization has begun the systematic transfer of activity from the public to the private sector. It is already a world-wide movement, and is still accelerating. It shows every sign of making widespread and irreversible changes to the distribution between public and private sectors, and thus becoming one of the most potent economic facts of our age. It is a world event whose effect has barely begun to make itself felt.

## PRIVATIZATION IN BRITAIN

There is no doubt that Britain has established a world lead in privatizing the state sector of the economy. Although it was not a feature of the 1979 election manifesto, privatization has come to be one of the most successful policies of the Thatcher period.

It was the comparative lack of success with alternative attempts to curb the growth and abuses of the public sector which led to the increasing use of privatization. The costs of government were not easily cut; cash limits were exceeded; wastage was not easy to identify and eliminate; and unnecessary programmes proved to be more durable than legislators had anticipated.

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The move to the private sector, on the other hand, proved itself as an immediate and popular success. Once they were privatized, former state operations rapidly became more efficient and more responsive, and no longer required losses to be met by taxpayers.

The government privatized British Petroleum in 1979 by declining to take up a share issue, thus allowing its holding to fall below 50%. Under the rules of the British Treasury, a company with over half of its stock in the private sector does not count as state-owned, and any capital it raises is not treated as part of the public sector borrowing requirement. British Petroleum was thus privatized indirectly, and started to operate as an ordinary commercial company, raising its capital on the financial markets, and trading on the basis of commercial, rather than political, judgements.

In quick succession the government sold British Aerospace, Amersham International and Cable and Wireless, rapidly developing the expertise required for stock flotation by the use of top city advisors. This was not achieved without criticism. If the share issue was over-subscribed, resulting in a premium for investors, the government was charged with selling national assets too cheaply. If the issue was under-subscribed, this, too, was called a failure.

Thus the Amersham sale was described as a bonanza for the government's "city friends" because the price attracted many buyers. The Britoil sale, on the other hand, was described as a flop because the price attracted too few. It seems that opponents of privatization expect a share issue price so exact as to generate no premium. It should be borne in mind that the government did in fact receive the money, even for Britoil, thanks to the use of underwriters to guarantee the deal.

As more public sector companies have been sold, so the government has gained the experience to handle the sales of all or part of their equity. It is more common for an initial sale to be of part of the stock, enough to effect the transfer to the private sector without making too high a demand on the capital market. Following privatization, further tranches of public equity are sold at a later date.



Because companies behave more competitively and more commercially in the private sector, their value after privatization usually rises, giving the government a healthy return on the subsequent sale of further stock.

The sale of British Telecom in December 1984 is instructive, in that successful attempts were made to attract large numbers of first time share owners. A huge advertising campaign was backed by the promise of reduced telephone bills over several years for share buyers. The purchase itself was offered in easy stages, with only a "down payment" initially required to buy.

Two million applicants bought shares, and two-thirds of those chose to retain the shares as an investment, despite the allure of quick profits from a high premium. In fact the sale was handled to achieve this. Small applicants were given priority. If less than 800 shares had been applied for, all were granted. Up to applications of 100,000, only a maximum of 1,600 shares were allotted, and beyond 100,000, none at all. This meant that large investors and funds which sought to include British Telecom in a portfolio had to buy in the market. Not surprisingly, this pushed up the price for the shares of the successful small applicants.

While Telecom was the largest single company thus floated, the sale of British Gas is estimated at twice the size, and when the water authorities are privatized, it will be even larger still.

One encouraging feature of the sales has been the growing level of public interest in them. When shares in Jaguar cars were sold in 1983, the city witnessed traffic jams and actual fights in the street as applicants struggled to get their bids entered on time. Clearly, the British public has taken to privatization and the revitalization which it promises for once state-owned operations.

While the first phase was dominated by easily-sold companies, the second stage has been dominated by the utilities. These require careful preparation and packaging, and are often marketed in novel ways. Thus the main headlines of the mid-1980s are made by telephones, gas, airlines, airports and water.

For some of these, a monopoly situation has had to be dealt with either by the establishment of a body to promote competition, or by opening up the various markets to small and specialist firms to offer alternate choices. Many of the requirements of the new private utility company are written into the act itself; others are left to competitive choice actively promoted by a new body. British Telecom, for example, has written specifications concerning the number of pay-telephones in remote areas and the cost of telephone calls in relation to the price index.

#### Sale to Workforce

In some cases the privatization has taken place not by sale to a private company, or by public flotation, but by a management and workforce buyout. National Freight Corporation was sold in this



way, with management and workforce pooling savings, and in some cases mortgaging their homes, in order to buy a stake. After four years their capital gain was in the region of 1,000%, with the company operating much more efficiently than it did in the public sector.

Some of the shipyards, notably Redhead, were sold to the workers themselves. In some cases this has called for novel methods of purchase, including special loans and extended payment sales. The cross-Channel hovercraft service was effectively given to its workforce.

#### Disposal of Subsidiaries

Even for state operations which cannot be privatized in their entity, the British government has found that viable sections can be sold independently. Thus for example, it has not been able to sell British Rail, but it has sold the 29 British Rail hotels, many of them to their workforce. It has sold the English Channel ferry services owned by BR to the private sector, and been able to privatize the British Rail engineering works and the BR hovercraft service.

In a similar way, parts of British Steel have been moved into the private sector. British Leyland is in process of privatization in stages. Following the successful float of Jaguar, the next moves involve the sale of Unipart, BL Trucks, including Landrover, and finally some of the main auto production lines.

An impressive total of sales has been clocked up as government of various levels has disposed of land and buildings surplus to need, and attention has been turned to the massive holdings in the hands of the Property Services Agency. Plans are in train for the similar sale of forestry lands.

#### State Houses

The biggest success of the privatization programme is probably not to be found among the ranks of industries and utilities. It is the sale of state-owned council houses to their tenants which has been largest in both effect and financial implications.

In 1979, some 35% of British houses were state-owned, occupied by tenants at subsidized rents. Previous attempts to raise rents to "economic levels" encountered resistance. The new privatization policy was to encourage purchase by sitting tenants at discount prices. Occupation for two years earned 20% off market value, and 20 years qualified for 50% off (later raised to 60%).

People leapt at the chance to become home-owners, and roughly 900,000 have bought. The programme is being extended to cover flats as well as houses, and sales are expected to rise yet more. Evidence so far suggests that houses, once bought by their tenants, are better maintained and last longer.



In financial terms, the yield from sales was by 1985 higher than that of all of the other privatizations added together. At over £12 billion, it was of major importance in the budgetary process. It was also one of the most popular of all of the privatization policies, with even the Labour Party forced to drop its initial opposition and embrace the programme with a "right to buy" policy of its own.

#### Contracting Out

In addition to the more public sales, a form of privatization has been spreading rapidly which involves the use of contractors from the private sector. Instead of continuing to use in-house labour, and to perform the service as an activity of government, the move has been towards inviting private businesses to bid against each other to perform the task. In this way the advantages of private sector production are obtained, even for those services which still fall within the overall responsibility of government.

Local government services have proved a fertile field. One after another, local councils have been contracting out the collection and disposal of garbage, the cleaning of streets, the care of parks and gardens, and a great variety of other services. Even the professional services of architects, lawyers and planners are included.

What started in Southend and was rapidly taken up in Wandsworth has now made an impact throughout Britain. Even councils which have opted not to privatize particular services have gained lower costs by simply considering the idea. Many have accepted lower bids from their own workforce trying to keep the service.

Typical savings fall in the range of 20-40%, right across the spectrum of services. More modern equipment and techniques are usually among the first fruits of privatization. The old council workforce are often given first chance at the new jobs created, and any not taken up are usually absorbed elsewhere within the local council.

The programme has made an impact upon every local authority in Britain, and has been extended into services for both schools and hospitals. Catering and cleaning jobs, formerly performed by the direct labour force, are now in process of being contracted out to private businesses.

At a national level, contractors are increasingly used to clean and maintain public buildings. They are used to service military bases. Throughout the public sector there is in process a general examination of all jobs performed to see where contractors offer the chance of savings and improved services.

#### Open to Competition

One very effective method of privatization has been achieved by opening up a state monopoly to competition, and permitting choice



to the general public. As the public select the private alternative, so they move an increasing proportion of the entire production over to the private sector.

The National Bus Company was exposed to this kind of competition on its inter-city bus routes. The competing lines cut the fares to one-third in some cases, and introduced service innovations such as video and vending machines. They captured a proportion of the trade, and now co-exist with the state operation.

The NBC itself responded to the competition with improvements of its own, and is itself scheduled for full privatization - in some cases to its own workforce.

There has been a dramatic rise in the use of private medicine in Britain, as private medical insurance has spread, together with the use of private hospitals. By 1985, the total spent on private medicine had risen from an insignificant proportion to £1 billion in total, compared with the £17 billion spent on the National Health Service. Furthermore, what had been a luxury service for people such as company directors, had become a normal recourse of several hundred thousand trade unionists.

The government gave slight encouragement to private medicine by making insurance schemes tax exempt for the lower paid. It is now probable that a little more incentive would lead to even more explosive growth of the private sector alternative. It certainly has been true in the pensions industry. Given attractive incentives to turn private, over 50% have already opted out of the state earnings related pension scheme, and chosen a private plan instead. This has made it possible for the government to reduce the scope of the state scheme even further. There is little doubt that privatization has a major contribution to make towards both choice and improved service in the area of the human services previously subject to an effective monopoly by the state.

#### The Pace Quickens

Economy campaigns on public spending tend to run into opposition and falter after a very short time. The same is not true of the privatization programme in Britain. Instead of reducing its scale it is increasing it. Each year sees more privatization than the previous one; some put the rate of increase higher than 50% per annum.

Privatization, which started so modestly, is now a significant component of the British budget. By early 1986, the yield from asset sales at the national level was running at £4.75 billion per year, equivalent to nearly 4% of income tax. The target list for the year includes big names such as British Airways, British Airports Authority, British Gas, Unipart, National Bus, Short Brothers, Rolls Royce, the Royal Naval Dockyards, and parts of British Leyland.

Norman Tebbit, Conservative Party Chairman, said that Britain in



1979 had the largest public sector of any country in the western world, but that by the early 1990s it would have the smallest. It seems certain that there will have been major and fundamental changes by that time. The Queen's speech of 1985 certainly made privatization a prominent and vital part of the government's programme, promising even more progress in future.

John Moore, the Financial Secretary to the Treasury, has pointed out that if the full programme is implemented, then the total proportion of gross domestic product taken up by state industries will have fallen since 1979 from 10.5% to 6.5%, with more than 600,000 jobs transferred to the private sector. He described the new phase of privatization as a cultural revolution, as it moved into "the heartlands of the public sector."

"Privatization has proved of such major benefit over the past five years," he said, "we have decided that it is right to extend it progressively to the so-called natural monopolies".<sup>2</sup>

Perhaps curiously, the demand from privatization has sometimes come from within the public sector itself. The National Freight Corporation buyout originated with the management. Now the management of the English Industrial Estates Corporation, which buys and manages factory developments in depressed areas, has proposed a management-led buyout.<sup>3</sup> The corporation's 320 staff in its 16 offices would be offered shares in the new company.

Lord Marshall, chairman of the Central Electricity Generating Board, has called for the privatization of the electricity supply industry in Britain<sup>4</sup>; and executives of the various water boards have been in the forefront of the drive to privatize the water authorities.

#### Teaching the World

Britain, so recently known as the "sick man of Europe," is leading the world. Other countries are turning to privatization precisely because of the success achieved in Britain. Dozens of countries have sent representatives to Britain to see the results at first hand, and to learn how it is done.

There is almost a "privatization tour" as they meet people from the newly-privatized industries, talk to the workforce, and meet with some of the customers. It is only a matter of time before some enterprising travel agent offers a package tour including visits to newly-owned council houses, and inspections of garbage collection done by private companies.

Britain has a world lead of several years in a movement which has begun to have global implications. The pace, moreover, is still accelerating. Disaffection with the economics of public sector supply may have gone further in Britain in 1979, but it has clearly spread to most parts of the world. Britain, which then experienced the problem at its most severe, has had the first experience of the solution.

No two countries have exactly the same type of public sector. In some cases it is the state industries which dominate, in others it might be the utilities. Some have a preponderance of state-supplied human services, and in others it is the regulatory function. Every country has a different mix, but Britain has shown that privatization can work in all of these areas, and has established some of the techniques which make it work.

There is thus a body of expertise in Britain of immense value to the rest of the world, and it is an experience which should be shared. As Britain's own economy changes over the years from a reliance on heavy manufacturing to the newer high tech and service industries, it could well be that its expertise in the practice of privatization will be one of its most sought-after assets.



## PRIVATIZATION IN EUROPE

Privatization as a major political force is no longer confined to Britain. Other western countries are taking up the strategy. In Europe privatization is catching on, though at a slower pace than in Britain.

On the edge of Europe, Turkey has sold the Bosphorus Bridge and the Keban hydro-electric dam, and has called in foreign consultants to advise on the privatization of a further 30 state concerns. The sale of the state airline, THY, is going ahead, and it is hoped that an initial percentage of THY equity will have been sold to its employees in the near future, with more of the equity being sold to the general public, and a final sale of shares to Turkish and foreign companies.<sup>5</sup>

The socialist-led government in Italy has also begun privatizing. The Italian state holding firm IRI has raised \$1.59 billion by selling some of its shares in various enterprises such as the Aeritalia aerospace company and the Selenia electronics firm. 40% of Sirti, a subsidiary of the STET telecommunications company was sold for L200 billion, and the state-owned Banco Nazionale del Lavoro, the largest bank in Italy, is offering 25% of itself to private investors, and more to its employees.<sup>6</sup>

The state airline, Alitalia, initially sold 10% of its equity to the public on the stock market, as part of a programme to place at least twice that much in private hands.<sup>7</sup> Italy's state energy group, ENI, has approved a second partial privatization plan for its Saipem oil and gas pipeline laying subsidiary. This will take the state holding down from 80% to 51%.<sup>8</sup>

In France the opposition has committed itself to a massive programme of privatization after its expected return to power. Privatization of almost everything nationalized since the second world war is being promised. And even the once strongly socialist Mitterand government is having to consider privatization.

Asked for her views on privatization, the former socialist hard-liner Mme. Edith Gresson, Minister for Industrial Redeployment, stated: 'I don't have a religious theory on this subject, neither for it nor against it...in certain cases I am not against diminution of state involvement in industry'.<sup>9</sup> Some parts of the large corporations which the French socialists nationalized, are already being sold. (Total losses of the French nationalized sector for 1984 have been estimated at Fr37 billion).

Nationalized Renault has been selling a wide range of assets from the company's prestige Champs Elysee HQ to Renix, an electronic component plant near Toulouse which was acquired by the American company Bendix. Nationalized Matra has sold its printed circuit subsidiary Comelin, and its experimental robot modules plant, Robotronics, both also to American buyers. Matra has sold its machine tools subsidiary MMA, and also plans on selling its car division and its loss-making watch division.<sup>10</sup>



Supposedly socialist Spain has started a privatization programme, with Socialist Prime Minister Felipe Gonzalez calling the bloated Spanish public sector a "white elephant graveyard." The national car manufacturer, Seat, has been sold to Volkswagen and plans have been announced to sell a state-owned ball bearings factory and to hive off sections of high technology firms.

It is thought that the state airline, Iberia, will soon also be privatized.<sup>11</sup> The state holding company, INI, has sold its textile firm Textil Tarazona, and sold its stake in the Spanish subsidiary of SKF to the Swedish parent company. The Spanish truck and bus-making firm ENASA has been sold to General Motors.

At a cabinet meeting on March 26th 1985 the German government examined 13 possible privatization schemes. They decided to concentrate on three general areas - industry, transport, and banking. Six companies are slated for privatization, including Lufthansa. A portion of the Berliner bank has already been sold, and two smaller banks, as well as facilities on the autobahn, trucking concerns, and tourist offices, are being readied for sale. In 1984 the German government reduced its shareholding in the Veba energy group from 43.7% to 30% by selling 4.4m shares.

The West German government now expects income of DM 2 billion in the next two years from part-privatization of state owned companies.<sup>12</sup>

The Social Democratic Prime Minister of Portugal, Anibal Cavaco Silva, has initiated a programme to end state domination of the economy, which he blames for keeping Portuguese living standards well below most of the rest of Europe. Presenting his privatization programme to Parliament he stated: "Nothing justifies our remaining on the bottom rung in Europe. We are determined to put an end to the resignation and impotence imposed by our giant state machine".

In Israel, a country with increasing economic links with Europe itself, privatization has appeared. Elta Electronics, a state-owned company which makes sophisticated military systems for military application, is soon to be floated on the Israeli stock exchange. The government is hoping to raise around \$13m from the initial issue, some 60% of which is expected to be taken up by the country's workforce.<sup>13</sup>

In Holland the transport minister, Mrs. Neelie Smit-Kroes, endorsed recommendations to break the monopoly of PTT, the Dutch Post and Telecommunications agency, thereby boosting proposals for its privatization. An advisory panel to the cabinet has meanwhile recommended the privatization of several partially or wholly state owned companies, including Hoogovens, the Dutch steel group.<sup>14</sup>

Even Denmark's coalition government managed a small feat of privatization. It sold the state's 50% stake in Kryolitselskabet Oeresund, a company which makes, among other things, biscuits.



The flotation was acclaimed as the biggest money raiser in the history of the Danish equity market.<sup>15</sup>

The pace in Europe has been quickening, as more and more nations have seized upon privatization as a means of disposing of state loss makers, and providing opportunities for private enterprise and initiative, as well as providing the kiss of life to state industries on the edge of survival.

Nowhere has privatization been undertaken, as it has in Britain, as part of a systematic programme. Despite this, the future is certain to see ever more examples of the diminution of the state sector in one country after another. Despite American forebodings, Europe is far from dead. On the contrary, it shows new signs of economic vitality; and privatization is proving itself as a very effective medicine.



## PRIVATIZATION IN OTHER ADVANCED COUNTRIES

Meanwhile, on the other side of the world, the Canadian government has decided to sell two loss-making state-owned airframe makers, Canadair and de Haviland, as well as mining businesses such as Eldorado Nuclear, a uranium producer. De Haviland is being sold to the Boeing Corporation for \$170m (\$98m for purchase and a \$72 million investment in on-going product development and modernization programmes at de Haviland's Toronto plant).

Canadian Arsenal, an arms manufacturing company, and Teleglobe Canada, which handles overseas telephone calls, will also be sold. In a statement announcing the privatization of these concerns Robert R. De Cotret, President of the Canadian Treasury Board and Chairman of the Ministerial Task Force on Privatization said that "a key element of the government's commitment to good management is our policy for the privatization of commercial crown corporations which no longer fulfill a specific public policy purpose."<sup>16</sup>

South Africa has turned to privatization as a means to invigorate her shaky economy. State intervention in and regulation of the economy have been heavy in South Africa. The public sector is a bastion of white privilege, with 46% of the 2.6 million strong white labour force being employed there. Now the South African government has set up a special committee headed by three cabinet ministers to draw up proposals for the privatization of public sector enterprises. President P.W. Botha revealed that the government had been carefully studying the UK privatization experience.

Three forms of privatization are under consideration: the transformation of state enterprises into public companies, with shares issued through the stock exchange; the purchase by private companies of state assets on a tender or private allocation basis; and a management buyout option under which the management and employees of smaller state undertakings would be encouraged to take over ownership.

Already the Sasol oil-from-coal corporation has been successfully privatized, and future privatization targets are expected to include South African Transport Services, (SATS), which runs the state airline, the rail network, harbours, and other transport services, Escom, the electricity supply corporation, and Iscor, the state steel corporation.

The Japanese have also begun privatizing their relatively small public sector. Legislation was passed in 1984 to transfer both the telecommunications system, Nippon Telegraph and Telephone, (NTT), and the state tobacco and salt monopoly, to the private sector.<sup>17</sup>

The profitable NTT became a private company on April 1st 1985, and its monopoly was ended. Although privatization was fought tenaciously by a combined bureaucratic and trade union lobby, the



government pressed ahead as it felt that continuation of the state monopoly would endanger the programme of long-term technological modernization.

Action is proceeding to privatize the loss-making Japan National Railways, (JNR), and it is hoped that the appropriate legislation will be passed by the end of 1986. The plan is to split JNR into six private regional firms and two national private firms. One of these will own the bullet train network and the other will own JNR freight interests. JNR'S substantial land assets will be sold to pay off some of its debts. The government hopes to divest itself of other loss-making concerns as part of a wider strategy to reduce state spending and the budget deficit.

Privatization has generally gained a good reputation in Japan, good enough for the Minister for Aviation to propose that it should be applied to Japan Airlines in order to restore public confidence after the 1985 747 jet disaster. The Council for Transport Policy, a government advisory panel, proposed in December 1985 that the Japan Air Lines monopoly on international routes be ended, and that Japan's two other airlines be allowed to compete on all international routes. This policy is seen as complimentary to the sale of JAL.

Australia is not exactly in the forefront of privatization, yet even here the Hawke government has made some limited moves. The Defence Service Home Loans Scheme has been marked for transfer to the private sector, and the government has sold the Belconnen Mall in Canberra.<sup>18</sup> The policy in Australia seems to be one of introducing privatization in a limited way at both state and federal levels, without using the name, and thereby avoiding any antagonism of Australia's entrenched and powerful unions. Even without the name, however, the rose smells as sweet.

The overall picture which emerges is that privatization is now a force whose effect has registered in all of the advanced economic powers. Some are willing, some reluctant. Some have touched it tentatively, others embraced it warmly. The remarkable thing is the consistency with which they are all turning increasingly to private sector alternatives. The variation is in the pace, and in the speed with which they are giving themselves access to its advantages.



## PRIVATIZATION IN THE UNITED STATES

The United States has come only recently to an understanding of the potential offered by privatization. Instead, the US has been following the more traditional attempts to cut government costs by curbing wastage and eliminating unnecessary programmes. Like others before them, they have achieved the traditional result.

Rather more innovative has been the United States' pursuit of supply side tax policies. They have sought to offer opportunities to the private sector by cutting tax rates, thereby extending the size of the tax base. On the whole, this has been successful in generating new business development and in creating new jobs. The US record at job-creation has been spectacularly better than that of other advanced economies. The federal deficit, however, has increased, and there has been no reduction in the size of the public sector.

Interestingly enough, privatization has made considerable impact in the United States, but mainly at the level of city services. Only now that the federal government is turning to privatization is there an appreciation of how much the American cities have set the pace, finding for themselves the same economies and improved services which privatization brings elsewhere.<sup>19</sup>

From garbage collection to landscape gardening, from vehicle maintenance to dog catching, the city governments in the USA have been turning to private contractors to perform public services under short term contracts. By 1984, the overall figures indicate how important a trend this had become:<sup>20</sup>

30% contracted out the operation and management of hospitals

35% contracted out day-care facilities

35% contracted out residential garbage collection

42% contracted the operation and maintenance of bus systems

44% contracted out commercial garbage collection

80% contracted out vehicle towing and storage.

In America today, private profit-making firms are under contract with cities to manage cemeteries, museums, parks, tennis courts, swimming pools, and arts and cultural centres. They also repair roads, control traffic, provide ambulance services, fight fires, provide crime patrol, and manage public works. In some cases they are entrusted with the entire management of city governments.

The striking feature of the list of services and functions undertaken by private contractors is its length and its diversity. There is hardly a single city service which is not handled somewhere by the private sector.



The reason for this widespread move toward use of private firms probably has its roots in financial pressures. Unlike budget-cutting operations which threaten closure of valued services, the privatization route retains the services but changes the method of delivery. In many, if not most, cases, the private firms combine lower costs with a more responsive service. This, in turn, places city legislators in a less pressured position.

City governments awash with cash rarely take the route toward privatization; they do not need to. But at a time when voters are resisting higher local taxes, and city budgets are under strain, few indeed are the cities so fortunate.

Analysts cite two factors as important in accelerating the trend toward the private sector. Firstly, there is an increasing use of sophisticated lobbying by well-heeled interest groups. They have become better organized and more skilled in exerting political pressure to pursue their interests. Secondly, there has been a cutback in federal subsidies, forcing city managers to look for more efficient and cost-effective ways of delivering services.

The use of private contractors is growing dramatically. More cities are using them for the first time, and cities which have already tried privatization are extending the number of privately delivered services. The decade from 1973 to 1982 shows growth in the use of contractors in virtually every region of city services across America.

Cities and Counties contracting with private firms

SERVICE	1973	1982
Ambulance service	169	303
Solid waste disposal	143	342
Refuse collection	339	486
Hospitals	57	108
Street Repair	63	444
Utility billing	104	161
Cemeteries	47	77
Data processing (records)	9	337
Payroll	65	172
Legal services	187	788
Public relations	30	108
Recreational facilities	7	123
Parks	5	142
Fire	2	15
Crime patrol	2	50
Traffic control	5	15
Museums	12	20
(Cities & Counties sampled)	2,375	1,780

(note: the columns are not exactly comparable because of differences in the sample base)



The impressive rise should not obscure the fact that the US still has a long way to go, even at the city level. Most cities have not privatized a great many of their services. Still, a few have shown how far the exercise can be taken with success. La Miranda, in California, has a population of 40,000. Despite this, it has only 55 employees, 23 perhaps because over 60 of its city services are now contracted out. A recently incorporated suburb of Dallas known, exotically, as The Trophy Club, has only one paid employee, a secretary.<sup>24</sup>

Of all of the methods of privatization at city level, contracting is reckoned to hold greatest potential for cutting costs. It is the competitive bidding, and the need to win contracts anew each time which keeps the firms lean and efficient. It is the need for public satisfaction which keeps the level of customer service high, and the need to cut costs which maintains innovation and keeps the service up to date.

Sometimes cities will use franchises instead of contracting. With franchises, the city can regulate the level of service, the quality, and even the price, but the consumers pay the provider, rather than the government.<sup>25</sup> They are most common for garbage collection and disposal, bus and airport operation, utility billing and meter reading, street light operation, vehicle towing and storage, ambulance service and emergency medical service. The franchise arrangement allows government to set standards, but turns the whole operation over to the private sector.

Many cities find that subsidizing a service provided by private entities is much cheaper than having the city provide the entire service itself. Thus Garden Grove in California saved roughly \$72,000 a year by turning its cultural arts centre over to a non-profit group, and paying them a subsidy to run it. The same city turned its youth counselling programme over to a non-profit group, halving the cost.<sup>26</sup>

Vouchers provide yet another alternative in which consumers are issued with a coupon which is valid for the purchase of particular goods or services. Although not frequently used, they have gained some successes. Their principal advantage is that the consumer can shop with them in the market place, with all of the benefits of competition.

Low income residents of Hennepin County in Minnesota can use city vouchers at any licensed day-care centre. Elderly and handicapped citizens are given transport vouchers in Kinston, North Carolina, to pay for taxi fares.<sup>27</sup>

The use of volunteers is effective in turning services wholly or partly into the private sector. There seems to be a large number of intelligent and able-bodied citizens prepared to give their services free to their fellows. Housewives, teenagers and retired people all form part of this pool.

Baltimore uses deputized volunteers to enforce sanitation and



building codes. New Orleans uses 3,000 volunteers in 85 different agencies throughout the city. Virginia Beach uses 100 volunteers in its libraries, saving \$42,000 per year; 3,000 volunteers in its recreation programmes; and even 150 of them in its police department.28

Studies which compare the cost of public and private provision in US cities show that only in the field of payroll preparation does the in-house service hold its own. In all other services studied, there is a significant cost-saving brought about by the move to the private sector.

An analysis of eight activities performed in 121 cities in the Los Angeles county area shows this effect:29

The Extra Cost of City Provision

SERVICE	% extra cost of city provision
Street cleaning	43%
Janitorial services	73%
Refuse collection	42%
Payroll preparation	0%
Traffic signal maintenance	56%
Asphalt overlay construction	96%
Grass maintenance	40%
Road maintenance	37%

(the cost differences are adjusted for differences in the scale and quality of service, and physical conditions under which the service is provided)

Firefighting is a service in which the same contrast emerges. The city of Scottsdale, Arizona, has a long-established and justly famous private fire service. Rural/Metro has been providing the service there since 1952. A detailed study ten years ago compared Scottsdale with three Arizona cities of comparable size.

Scottsdale was way ahead in terms of cost-effectiveness, with an average annual cost of \$6.48, only 56% of the \$11.58 per capita cost for the other cities. The innovatory methods of Rural/Metro pioneered the mix of full-time and reserve firefighters now being copied elsewhere in America.30

The escalating costs of keeping criminals in prison has led several states to turn to the private sector for the construction and operation of prisons. There is a growing list of US firms who are offering correctional services.31

One of the first was the Nashville-based Corrections Corporation of America. CCA started with two correction centres: a community facility for juveniles in Memphis, and a processing centre for illegal aliens in Houston. It now runs two prisons in addition. One of them, the Hamilton County goal in Chattanooga, is a 360-bed prison run on a four year contract. CCA charges the county



\$21 per inmate per day, compared with the county's bill of \$24 when it ran the prison itself. Moreover, CCA have done this while improving both standards and services, and spending \$3.5 million on renovation.

The other goal is a 196-bed facility in Bay County, Florida, and is on an eight year contract which involves extending it by a further 150 beds. This will bring CCA's total to 1,500 beds, although they are pursuing contracts involving 14,000 beds. They reckon their average saving to be between 10% and 15%, and are now marketing their services all over America.

Other significant examples include a 720-bed penitentiary outside of Pittsburgh, which Buckingham Securities has won approval to proceed with, and an experiment in Minnesota in which a nonprofit data processing firm leases space in prison, and hires the inmates to do programming.

Privatization in the US has now made inroads into water services. San Diego's water authority buys from a private supplier. Twin Falls in Idaho has turned its sewage treatment over to the private sector, and some areas now use private firms for reading the water meters.

Perhaps the ultimate service is city management itself. One Florida entrepreneur has won contracts with two municipalities there to provide management, administration and even clerical services. A rival offer Florida cities private management and administration, and is winning contracts.<sup>32</sup>

The Management Services Institute of California offers cost-accounting analysis to California cities. Another firm manages public works operations in the same state. Others supply building and safety, engineering and planning services on a contract basis, and one actually supplies the city engineer.

Important though privatization has been at the local city level, it has made little impact elsewhere. The American states have not made significant progress, and there has been negligible activity at the federal level. A possible explanation is that a widespread view in the US sees privatization only as a budgetary help. Its role in reducing the private sector, in making services more cost effective and more responsive, is not widely appreciated.

The prospects, however, are promising. As the US administration finds the public sector recalcitrant when cost-cutting attempts are put in train, so it begins to see the possible merits of an alternate strategy. As it does begin to turn its attention to privatization, it finds a wealth of practical experience and success gained over the years by its own cities, and thus has the basis for some expertise. Privatization, so large in Britain's economy story, is only beginning its effect in the United States.



## PRIVATIZATION IN COMMUNIST COUNTRIES

A spectre is haunting the communist world - the spectre of free enterprise. Privatization is now being carried out in communist countries. Cuba is a good example. According to Senor Flavio Bravo, president of Cuba's national assembly, Cuba has "grave housing problems, many of them created by ourselves".

A new law passed by the Cuban national assembly privatized the majority of public housing this year. Under this law state tenants who paid about 10% of their income in rent had the ownership of their homes transferred to them, subject to a 20-year mortgage with the People's Savings Bank. Up to 15 years of repayments will be deducted for years of rent already paid and mortgage payments will roughly match current rents.<sup>33</sup>

A programme of sale of state-owned homes has also started in China. A limited number of houses are being sold in each city. For example six thousand flats were on sale in Shanghai last year, but buyers had to find a third of the 18,000 yuan (£4,000) price. The balance is paid jointly by the state and employer. The Shanghai municipal authorities are also launching a lottery for would-be house owners as part of a campaign to stimulate savings. Half of all the households in the city of 11 million have opened savings accounts which entitle them to lottery tickets and the chance of winning a new flat.<sup>34</sup>

A rather looser ideological attitude has been evident in China since the accession to power of Deng Xiaoping, an attitude based on Deng's famous saying: "It doesn't matter if a cat is black or white as long as it catches mice". It is certainly evident to Deng that socialism is a very bad mouse-catcher, and he has begun to dismantle it.

There has been an explosion of private enterprise. Privately-owned restaurants and shops have been starting up since 1978 at four times the rate of their state counterparts. A whole street in the Manchurian city of Harbin is given over to the sale of new privately-made vinyl sofas, and similar free markets can be found in cities such as Canton, Shanghai and Chengdu.

Even the principle of state ownership of land is now under attack. A recent national symposium heard some speakers argue in favour of privatizing state land. They alleged that current "building costs and rent regulations are quite unrealistic. The more buildings you erect the more money you lose."<sup>35</sup>

In Hungary private food production is nearing half of the total, and a growing number of private businesses are starting up. People invest for profit, and now even lease state factories to run them for private gain. A system of bidding has even been introduced for the right to run private businesses. Says Zoltan Palmai, the owner of the new Victoria Hotel in Budapest, the only private hotel in the Soviet bloc, "only private enterprise can save our economy."<sup>36</sup>



Even the Soviet Union itself has experimented tentatively with privatization. In Estonia in the summer of 1985, some radio and TV repair services were turned into worker-run profit-oriented enterprises. The result was that radios and televisions were repaired in less than two days, instead of the usual two to three weeks. Similar experiments are now being carried out with other service sector jobs.<sup>37</sup>

Soviet Chairman Gorbachov's speech to the 1986 Party Congress suggests that innovations will probably include the introduction of more incentives derived from the private sector, in an attempt to revitalize the excessively bureaucratic framework which restricts the economy.

What these examples from the communist bloc demonstrate is that there are no limits to privatization possibilities. Throughout the world central planning has been revealed as a failure. It neither delivers the goods, nor does it any longer provide the motivation. Although in some instances the rhetoric may linger on, most countries will want to dismantle their socialist institutions and policies.

On the available evidence it would not be an exaggeration to say that the next decade will see a privatization revolution sweep the world. It is already well under way. Although it will clearly take longer than ten years before the privatization of the Soviet Post Office, to the Adam Smith Institute at least this is a long-term goal.

Some analysts even speculate that the centrally planned system itself may be on the way out, replaced by one in which the communist party will determine the overall priorities, but allow such factors as production, management, and even price to be determined by the supply and demand signals which characterize the free economies.



## PRIVATIZATION IN THE THIRD WORLD

Asia is probably making the most progress, outside of Britain itself, in privatizing.<sup>38</sup> In Sri Lanka, Finance Minister Ronnie de Mel has stated that the government has taken a policy decision both to refrain from going into any activity that the private sector can do better, and to hand over to the private sector some activities now run by the state. The telecommunications system is up for sale, and the country's buses, formerly a monopoly of the Ceylon Transport Board, have been deregulated and privatized. Some loss-making textile mills were also sold, and are now making a profit in private hands.<sup>39</sup>

Bangladesh has sold off nearly 100 companies, including most of the jute, textile, chemical, and engineering industries, since the announcement of a New Industrial Policy in 1982.<sup>40</sup> There are plans to sell via the stock exchange up to 49% equity stakes to private investors in state-owned banks, shipping lines, the national airline, and the telephone system. Foreign investors will be allowed in.

India's new prime minister, Rajiv Gandhi, has said that the public sector "has spread to too many places where I feel it should not be". The government has set its face against any more takeovers of "sick" industrial units in order to save jobs, and will sell or close down 26 "sick" state-owned textile mills. It has also decided to involve the private sector in areas until now solely a state preserve. For example in June 1985 the central government asked state governments to consider involving the private sector in laying express toll highways as an alternative to the existing highways which are toll free.

Pakistan has privatized some 2,000 rural rice, flour and cotton mills, and contracted out the maintenance of small wells and irrigation projects to the private sector. Finance Minister Mahbubul Haq is a champion of privatization and is planning to sell shares in a variety of government-owned corporations. The government is hoping that revenue from privatization will become a major source of revenue and help it reduce its reliance on deficit financing. The budget for the fiscal year 1985-86 relies in part on privatization revenues.

Malaysia's public sector has reached unmanageable proportions, and the government has now committed itself to extensive privatization. The Malaysian Telecommunications Department will be turned into a government-owned corporation which will then hive off selected functions to the private sector. The government has had lengthy talks with British merchant banks and stock-brokers about ways of achieving full privatization of Telekom.<sup>41</sup>

The Malaysian Airlines System, (MAS), will become a private corporation over a period of three years; 30% of the shares were sold in October 1985. A joint government/private company, Aerospace Industries Malaysia, will take over the air force's maintenance facilities.



The sale of the country's power stations is under consideration, and the government seems to be committing itself to at least partial privatization of the state oil company, Petronas.42

A bypass road in the Kuala Lumpur area has been leased to a private company, Shapadu, which will manage the road. In addition to all this, a number of services are being contracted out. For example, waste management services in Kuala Lumpur have been contracted out to a British firm, GIS Waste Services. The government also intends to sell hotels, car parks, a lottery, water supplies, and a container terminal near Kuala Lumpur.

Singapore is retreating from the state capitalism that has been an important hallmark of its economy. The government has adopted a policy of seeking listings on the Stock Exchange of Singapore (SES) for public sector companies whenever possible, and of selling through the SES the majority of its minority stakes in companies.

An early privatization candidate will probably be Mitsubishi Singapore Heavy Industries, which is involved in shipbuilding and repair. A tentative agreement has been made to sell the government's 44% stake and the 5% stake held by the State-owned Development Bank of Singapore (DBS) in this firm to Mitsubishi Heavy Industries of Japan.

In November 1985 16% of the equity of Singapore Airlines was sold, with many of the shares being bought by the airline's employees, who already owned 23% of the shares. The programme calls for at least half the offered shares to be allocated to the public in Singapore, with the balance placed in London, New York and Sydney.43

Other likely candidates for privatization are DBS itself, DBS Land, Singapore National Printers, Singapore Shipbuilding and Engineering.

The government has also announced its intention to sell its hotel interests, which include Hotel Premier and a large holding in the Raffles City development. The state's 45% investment in a local subsidiary of the British food group Rank Hovis McDougall, has been sold. The retreat from Singapore's 'nanny state' can be expected to gather momentum.

In the Philippines the public sector constitutes a major drain on the nation's resources. In the current year the 15 biggest state corporations are expected to incur a combined loss of some \$542m. The previous government began a process of privatization which the new administration is expected to continue. Firms to be privatized in the near future include the Commercial Bank of Manila, the International Corporate Bank, the Philipinas Bank, Resort Hotels Corporation, the Bataan Pulp and Paper Mills Inc., and Delta Motor Corp.



In Thailand a privatization programme has started despite strong opposition from vested interests, including retired military officers appointed to the boards of many state corporations. In January 1985 the government decided to privatize parts of the Electricity Generating Authority of Thailand and Thai Airlines International through the stock market. It also is trying to privatize Bangkok bus operations and part of the phone system.

Between 1982 and 1983 the South Korean government divested itself of all nationwide commercial banks. Competition in the financial sector was further encouraged by the licensing of 43 new private mutual savings and finance companies and 10 short-term finance companies. Some public enterprises such as the Korea Oil Company and Korea Heavy Industry were also sold.

The Koreans are proud of the success of privatization in the manufacturing and service areas. Among those divested have been Korean Airlines, Daweoo Heavy Industry and Yukong Inc. These enterprises are reported to be operating more profitably and more efficiently since government totally relinquished management.<sup>44</sup>

Privatization is beginning to make inroads in the new world. The new president of Brazil, Jose Sarney, has announced a major change in economic policy towards privatization and promotion of the private sector. "Rarely in our history have we had such an opportunity to change the nature of of Brazil's economic process", he has declared. "Leadership of the economic development process should now pass to a private sector freed from the shackles of statism".

President Sarney has accepted the sales list of 89 public sector companies identified by the previous government headed by General Joao Figueiredo. Of these 20 had been sold and 27 had been merged or handed over to local authorities. Sarney will sell the remaining 42 as well as a further 12 which he has himself identified.

The new Brazilian government's first task has been to find out the extent of the public sector, which has spread so widely that no-one quite knows its full size. So far more than 20,000 federally-owned companies and official bodies have been found, but this is by no means anywhere near the total.

The Brazilian privatization programme is likely to take three forms. State-formed companies which play no strategic role in the economy, usually service or supply subsidiaries of large corporations, will be privatized. Former private sector companies which were taken over by the government due to financial difficulties will also be sold off, or transferred to state and municipal government, or even closed.

Private capital will be introduced into the large state corporations, such as the Petrobras oil monopoly, the Valo do Rio Doce mining company, the Eletrobras electricity utility, and the Siderbras steel company.



The first moves were made in November 1985, when small investors in Brazil were given the opportunity to buy stock in Petrobras in a share issue which raised about \$400 million.<sup>45</sup>

Jamaica has sold or leased most of its sugar refining and hotel interests.

Mexico in March of 1984 privatized 73 of its 467 nationalized companies, including the Telephone Company of Mexico and an affiliate of John Deere. On February 6th 1985 the Mexican cabinet decided to "liquidate, dissolve, merge, transfer or sell 236 state companies and agencies over the course of the year. So far, however, only 31 of the 236 have actually been put up for sale, together with minority government interests in another 13 companies.

One of the most significant sales was that of the Nacional Hotelera chain on October 28th 1985 to a private Mexican investment group backed by two state banks as minority partners. The purchase price was set at 27.2 billion pesos, which is \$84m at the official exchange rate.<sup>46</sup> The Mexican privatization drive, hesitant though it may be, represents a reversal of the policy of public sector expansion which had been pursued for the previous 12 years.<sup>47</sup>

Extensive divestiture has occurred in Chile, where 13 corporations and 18 banks were sold between 1974 and 1983. In 1981 Chile privatized its pension system, creating ten Administrators de Fondos Previsionales, (AFPs), providing old age, sickness, maternity, health and other insurance. Shares of these AFPs are now being sold, as are shares in the power company, Chilectra, and two large banks the government was obliged to take over after their collapse in 1983. A genuine capital market is emerging and share issues are increasingly popular.<sup>48</sup>

Even in New Guinea, the new government was reported in November 1985 as being likely to deregulate the aviation industry, and to sell off Air Niugini as part of its commitment to privatization.

What is remarkable about the progress of privatization in the third world is its diversity. Virtually no country remains unaffected by it. The range of industries and services which it has already touched is astonishing, although it is clearly still in its very early stages.

No less remarkable is the ease with which the third world finds itself able to privatize. It could be that the public sector operations there have not put down the deep roots of their counterparts in the advanced economies, and that the interest groups which depend on the state sector are not as deeply entrenched, nor as experienced in their ability to manipulate the political process to their own advantage. Certainly, apart from Britain, it is in the third world that privatization has made its biggest inroads.



There is some irony in the fact that a large part of the third world learned the wrong lessons originally from Britain. It was from Britain that their educated class learned to think in terms of state activity and investment. Central planning and socialist controls have by no means proved a welcome legacy to countries which seek economic expansion and a space for enterprise to operate.

Fortunately for the wealth creating process, the wheel has turned full circle. It is from Britain now that they receive the ideas behind privatization and the expertise which makes it possible to achieve successfully. By staking out an early lead, Britain has gained a start of several years on the rest of the world. They are now learning, sometimes painfully, what Britain already knows from its own experience.

The lead in privatization puts Britain into a good position in the rush to economic modernization. The race to turn the older economies, dominated by large-scale state-bound enterprises, into the newer, faster, more flexible systems, is on. Britain has a lead which stands her in good stead to take a commanding position in the coming century, if she keeps up with the policy and continues to accelerate the pace of it.

Meanwhile, as the Financial Times put it:

"Everywhere the State is in retreat."



### Footnotes

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