

MIT Course 11.946 Planning in Transition Economies for Growth and Equity
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Discuss the challenges of privatizing state-owned enterprises in the transition countries – what extra challenges might they face compared to other countries?

The challenges of privatizing state-owned enterprises in some transition countries could be reviewed through results of privatization reforms, which received a very negative score and opinion. For example, the Russian privatization program is criticized that 1) privatization was implemented too rapidly without appropriate institutional preparation and legislation; 2) privatization weakened state power, eroded public order, and caused corruption; 3) privatization did not create real owners of property, and, in fact, all (or almost all) the property that was privatized had a criminal element (See, for example, Stiglitz J. Whither Reform? Washington D.C.: The World Bank, 1999)

Though the reality in Russia as well as other transition countries was very specific and different from what its critics saw, I agree that “there are some important preconditions that have to be satisfied before privatization can contribute to an economy’s growth (Stiglitz J. Globalization and its Discontents. W.W Norton& Company, 2003).

According to conclusions made by William L.Megginson and Jeffrey M.Netter in their survey “From State to Market: A Survey of Empirical Studies On Privatization” (Journal of Economic Literature 39 (2):321-389) “it has been clear that the success of the privatization program depends on the strength of the markets within the same country, and vice versa”. Thus, they emphasize, ‘the impact of privatization will differ across countries depending on the strength of the existing private sector’. It is also mentioned that the effectiveness of privatization depends on institutional factors, such as the protection of investors.

One more very important issue raised by all the authors of the assigned readings (as well as by many critics of market-oriented reforms in transition economies) is the impact of privatization on employment I agree that privatization leads to restructuring, which means the destruction of unproductive jobs, which are replaced by new more productive jobs (These ideas are considered by Bilson V. in “Job Creation, Job Destruction, and Growth of Newly Established, Privatized, and State-Owned Enterprises in Transition Economies: Survey Evidence from Bulgaria, Hungary, and Romania”, Journal of Comparative Economics 26 (3):429-445).

But I would like to emphasize the problem of so-called “social costs” associated with unemployment, which private firms often do not take into account. Privatization has been so widely criticized because privatization often destroys jobs rather than creating new ones. According to J. Stiglitz, “in industrialized countries, the pain of layoffs is acknowledged and somewhat ameliorated by the safety net of unemployment insurance. In less developed countries, the unemployed workers typically do not become a public charge, since there are seldom unemployment insurance schemes’ (Stiglitz J. *Globalization and its Discontents*. W.W Norton& Company, 2003, p. 57).

The general conclusion is that attempts of privatizing state-owned enterprises in many transition countries were failed because privatization had not been considered as a part of a more comprehensive program aimed to build appropriate institutions and create preconditions for successful privatization’.

References:

1. Assigned readings for March, 1, 2004 Class
2. Stiglitz J. *Whither Reform?* Washington D.C.: The World Bank, 1999.
3. Stiglitz J. *Globalization and its Discontents*, W.W Norton& Company, 2003