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Why Haven't Developing Countries Privatized Deeper and Faster?

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Summary. — Despite a decade of privatization in the developing world, the vast majority of state-owned enterprise (SOE) assets continue to be in government hands. *Bureaucrats in Business* (World Bank, 1995) correctly identifies politics as one reason for the slow pace of privatization but it underestimates the role of institutional and economic constraints. Success stories of privatization are rare in low-income countries, and the long-term promise of privatization in sectors posing regulatory complications remains to be established. Countries in crisis may reform SOEs quickly and deeply despite these uncertainties, but others may opt for gradual reform, which need not be altogether bad. If speedy privatization results in poorly conceived schemes, the cure can be worse than the illness. Finally, bureaucrats are likely to stay in business for years to come, and therefore it is important to improve their effectiveness in the roles they are unlikely to shed in the future. A market-friendly approach to SOE reform need not be government-*un*friendly. © 1998 Elsevier Science Ltd. All rights resrved.

1. INTRODUCTION

Given all the press about privatization in developing countries, the title of this paper may be surprising. If anything, it would appear that in the last decade developing countries of all stripes have been privatizing vigorously, and that some among them have been privatizing just about everything in sight. But *Bureaucrats in Business*, the World Bank's (World Bank, 1995) high-profile study of state-owned enterprises (SOEs) reform in developing countries, expresses puzzlement at the *slow* pace of privatization. Its opening words read:

> Bureaucrats are still in business. Despite more than a decade of divestiture efforts and the growing consensus that governments perform less well than the private sector in a host of activities, state-owned enterprises account for nearly as large a share of developing economies today as 20 years ago. Indeed, as data compiled for this study show, the size of the state-owned enterprise sector has significantly diminished only in the former socialist economies and a few middle-income countries. In most developing countries, particularly the poorest, bureaucrats run as large a share of the economy as ever. (p. 1).

These opening words are loaded with debatable assumptions:

—that SOEs are run by bureaucrats, when in fact most SOEs are separate from and independent of the government and the civil service;

—that divestiture will take bureaucrats out of business, when in fact many of the industries in which SOEs operate require regulation after privatization; or

—that there is a consensus on the superiority of private over public ownership, when in fact this assumption is hotly debated in most countries, perhaps not in the abstract, but when applied to particular markets and activities.

I will explore these and other assumptions in this article, but will first address the more straightforward assertion in the above quote that SOEs have not shrunk much in importance in developing economies in the last 20 years. Since the statistical data in *Bureaucrats* was a few years old even at the time of the report's publication (World Bank, 1995), is

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that assertion still true? If yes, why so, and what might be done about it?

2. HOW DEAD IS THE STATE-OWNED ENTERPRISE?

One of the useful contributions of *Bureaucrats* is the statistical appendix on SOEs for 1978–91. Looking at that data, one would hardly be able to tell that SOEs in the developing world were being privatized. As the report notes, in low-income developing countries, the share of SOEs in GDP seems fixed in that period at about 14%, while in middle-income developing countries it oscillates between 8% and 10%, a level comparable to that in the industrialized world (World Bank, 1995, p. 34).

Because many developing countries began to privatize vigorously only after 1988, however, one might expect more recent data to tell a different story. Table 1 shows that the absolute sums of money raised by governments through privatization did increase dramatically over 1988–96 (the last year for which detailed information was available at the time of writing). One can also see that privatization took off first in Latin America and the Caribbean, followed by Europe and Central Asia and the East Asia and Pacific regions, while it proceeded at a slower pace in regions such as South Asia and sub-Saharan Africa. But Table 1 does not answer the more interesting question of how much the SOE sector has shrunk *relative* to its original base in various countries. Since the World Bank has not updated the statistical information in *Bureaucrats,* and there is no other international database on this topic, one must resort to crude estimates.

Table 2 presents one such estimate that compares the value of assets privatized in developing countries during 1988–96 with the value of government holdings in SOEs before privatization began. This estimate is based on assumptions about the ratio of capital stock to value-added by SOEs, and the ratio of the market value of government holdings in SOEs to their capital stock. Suffice it to say that while the assumptions have some justification, the estimate is very rough. It shows that only about 9% of SOE assets in the developing world may have been divested by December 1996. Even allowing for the possibility of systematic underestimation, the proportion of assets still state-owned appears to be substantial.

Table 3 applies the same method to obtain ballpark estimates of the proportion of SOE assets privatized in individual countries for which data were available. These estimates are good enough only to distinguish the deep privatizers from the shallow privatizers. At the "deep" end are countries such as Argentina, Bolivia, Philippines, and Peru that had privatized half or more of their SOE assets. Then come countries such as Ghana and Malaysia that had privatized one-third of their SOE assets, followed by Mexico that had privatized about one-fourth. At the "shallow" end are countries such as Brazil, Pakistan, Sri Lanka, and Turkey that had privatized in the low double-digit range, and India, Indonesia, and Nigeria that had privatized in the single-digit range. What these figures show is that some countries have indeed privatized much more deeply than others, and if the absolute percentages are reliable, they also show that some of the deep privatizers may have very little left to privatize. Data from other sources corroborate the guesstimates in Table 3.[1]

I have not attempted similar estimates for transitional economies, since data on privatization are less complete for these countries, and the relation between book and market values of equity is likely to be even murkier in their context.[2] But individual studies estimate the proportion of economic activity that has been privatized in countries such a Czech Republic, Hungary, and Russia at 50% or more (Spulber, 1997, p. 168). These numbers, however, should be taken with a pinch of salt. In the Czech Republic, for instance, almost half the shares in "privatized" firms belong to the National Property Fund or to voucher funds controlled by state-owned banks.[3] Even as late as 1996 only small service businesses had truly passed into private hands, while many medium and large SOEs continued to be state controlled, either directly or indirectly.[4] Therefore, even in 1996, the state accounted for 40–50% of GDP in countries such a the Czech Republic, Hungary, and Poland. This level of state ownership is two to three times the average, and a bove the upper end of the range, for the poorest developing countries (e.g., Guyana, Sudan, Zambia).

In summary, then, the privatization cup can be described as either half-full or half-empty, depending on one's point of view. Given that SOEs grew in importance for four decades after WWII, the mere fact that in one decade

Table 1. *Privatization in developing and transitional economies by region and year, 1988–96 US$ Million*

Region	Year									Total
	1988	1989	1990	1991	1992	1993	1994	1995	1996	
Latin America and the Caribbean	2530	1436	7297	17,989	15,797	10,646	7818	4623	14,143	82,641
Europe and Central Asia	27	685	1304	2783	4341	4151	2879	8937	5466	30,591
East Asia and the Pacific	21	196	376	835	5161	7155	5507	5447	2679	27,123
Middle East and North Africa	7	14	2	17	70	627	567	657	1477	3510
South Asia	na	3	29	996	1557	974	2666	159	899	8028
Sub-Saharan Africa	10	683	74	60	191	648	792	544	745	3861
Total	2594	3017	9013	22,761	26,761	24,200	20,228	21,116	25,399	155,753

Source: Compiled from World Bank (1998), Appendix 4.

Table 2. *Proportion of SOE assets privatized in developing countries, 1988–96*[a]

Region	GDP, 1992 ($B)	SOE share in GDP, avg. for 1985–87 (%)	Value-added by SOEs,[b] $B	Market value of govt's equity,[c] $B	Total proceeds from privatization, 1988–96, $B	Percentage of SOE assets privatized (%)
Low-income economies, excl China and India	427.6	13.8	59.0	177.0	na[d]	na
India	214.6	13.5	29.0	87.0	na	na
Middle-income economies	3549.0	10.3	365.5	1096.5	na	na
Total of above	4191.2	–	453.5	1360.5	125.2	9.2

[a]Excludes transitional economies.
[b]Value-added by SOEs (column 4) is the product of the previous two columns.
[c]Market value of government's holdings in SOEs is calculated through a two-step process. First, the value of SOE assets is estimated on the basis of an average ratio of value-added to capital stock of 6:1, a ratio obtained from Brazilian data on SOEs (see Trebat, 1983, p. 158). Second, we assume that the market value of the government's equity equals its book value, which in turn equals half the value of the SOE's capital stock (i.e. we assume a debt to equity ratio of 1:1). The second assumption is particularly shaky because the market value of the government's equity depends as much on regulatory policy, general investment climate, and the timing of divestment, as it does on the book value of the government's equity. Unfortunately, there is no way to incorporate these variables into the estimation procedure.
[d]na = not available.
Source: Compiled by author using data for column 2 in World Bank (1994) and for column 3 in World Bank, 1995, Table A.1. Data for cumulative privatization in developing countries are from World Bank (1998), Appendix 4. Remaining values were calculated using the above assumptions.

Table 3. *Proportion of SOE assets privatized in selected developing countries, 1988–96*

Country	GDP 199 2 ($B)	Share of SOEs in GDP (%)	Value-added by SOEs ($B)	Estimated SOE assets ($B)	Estimated mkt value of Govt. equity SOEs ($B)	Proceeds from privatization, 1988–98 ($B)	Percentage of SOE assets privatized (%)
Philippines	52.5	2.6	1.37	8.19	4.10	3.42	83.52
Peru	22.1	8.5	1.88	11.27	5.64	4.46	79.14
Argentina	228.8	5.5	12.58	75.50	37.75	18.25	48.34
Bolivia	5.3	11.4	0.60	3.63	1.81	0.81	44.69
Ghana	6.9	9.3	0.64	3.85	1.93	0.62	32.21
Malaysia	57.6	17	9.79	58.75	29.38	9.16	31.18
Mexico	329	13.1	43.10	258.59	129.30	27.32	21.13
Brazil	360.4	7.6	27.39	164.34	82.17	9.66	11.76
Côte d'Ivoire	8.7	5.1	0.44	2.66	1.33	0.15	11.27
Pakistan	41.9	11.5	4.82	28.91	14.46	1.58	10.93
Sri Lanka	8.8	10.4	0.92	5.49	2.75	0.29	10.56
Turkey	99.7	10.1	10.07	60.42	30.21	3.0 8	10.20
Venezuela	61.1	19.4	11.85	71.12	35.56	2.51	7.06
Chile	41.2	15.7	6.47	38.81	19.41	1.3	6.70
Indonesia	126.3	15.8	19.96	119.73	59.87	4.01	6.70
Nigeria	29.7	13.9	4.13	24.77	12.38	0.76	6.14
Thailand	110.4	5.4	5.96	35.77	17.88	1.04	5.81
Morocco	28.4	17.7	5.03	30.16	15.08	0.86	5.70
India	214.6	13.5	28.97	173.83	86.91	4.45	5.12
Bangladesh	23.8	2.5	0.60	3.57	1.79	0.06	3.36
Egypt	33.6	27.2	9.14	54.84	27.42	0.68	2.48
Zambia	3.8	29.5	1.12	6.73	3.36	0.07	2.08
S. Africa	103.7	15.5	16.07	96.44	48.22	0.64	1.33
Tunisia	13.9	30.2	4.20	25.19	12.59	0.13	1.03
< vsp sp = "0.5"							
Total above	2012.2	13.26667	266.95	1601.71	800.86	95.31	11.90

Source: Calcul ated by author using data and assumptions listed in Table 2.

they have shrunk by 10–15% in mixed-economy developing countries and by 30–40% in some transitional economies, is a significant reversal of the pendulum. Moreover, so many developing countries seem to be on the threshold of implementing ambitious privatization programs. OECD estimates the volume of privatization in developing countries in 1997 at $55 billion, or more than double the 1996 volume (The Economist, 1998, p. 125). Privatization in the developing world may well be following the familiar S-shaped diffusion curve, and by 1997 it may have reached the take-off point.[5] On the other hand, what remains under state ownership in many countries is substantial enough to frustrate ardent supporters of privatization such as the World Bank.

Thus, although privatization has accelerated in developing countries, two assertions made in *Bureaucrats* about privatization in developing countries were true even in 1996. Privatization was still concentrated in a handful of middle-income and socialist countries that had privatized deeply, and it was languishing in most of the rest of the countries.

Why have the majority of developing countries been pussyfooting on privatization? The answer in *Bureaucrats*, if one were to paraphrase, is that although privatization is good economics (Chapter 2), only rarely is it also good politics (Chapter 4). While both halves of this argument have merit, they are made much more strongly in *Bureaucrats* than the evidence seems to warrant. Moreover, *Bureaucrats* pays insufficient attention to historical and institutional factors that determine the desirability or feasibility of swift and deep privatization. We begin with a discussion of the political obstacles to privatization.

3. IS PRIVATIZATION BAD POLITICS?

The good news about the chapter in *Bureaucrats* on the politics of SOE reform is that it exists at all in a World Bank study. Previous Bank studies on SOE reform have assiduously avoided references to politics, even though most people inside and outside the Bank have recognized its crucial importance in shaping economic policies. *Bureaucrats* also does a fine job of identifying several variables that can help gauge a country's political readiness to privatize. The bad news is that the proposed model is static and its power to explain and predict political readiness for SOE reform are greatly exaggerated.

Bureaucrats begins with the familiar argument that because potential losers from privatization are better organized and more vocal than potential winners, privatization is usually bad politics — an argument widely made in the 1980s to explain the huge gap between the rhetoric and reality of privatization. But that argument cannot be made in the 1990s without finding a way to accommodate the many cases in which privatization has indeed been deep and swift. *Bureaucrats* attempts to explain these exceptions by introducing the notions of political desirability, political feasibility, and credibility. Although reform is often politically undesirable and infeasible, it argues that

> reform becomes desirable to the leadership when the political benefits outweigh the political costs, … [when] leaders have the means to implement change and to withstand opposition to reform, [and when] promises central to state-owned enter prise reform [are] credible (p. 10).

While this framework has some explanatory and predictive value, it also suffers from major limitations. First and foremost, it is a static model, whereas reform programs are dynamic and evolve over time. The interesting question usually is how reform programs unfold in various countries, and why they do so at faster rates in some than others. Second, political desirability and feasibility are not independent conditions, because they jointly determine the net political benefits of reform. Desirability depends partly on how feasible a reform is, and on the political cost that leaders must incur to make a reform feasible. Similarly, credibility is not a always a given, but can be created. Argentina and Mexico used the privatization of large SOEs, like the telephone company and the airline, to *create* credibility for their reform programs, rather than wait for credibility to somehow emerge before privatizing. Third, the role of leadership is completely overlooked in the *Bureaucrats* framework. Yet, it is clear from looking at cases such as Argentina, Mexico, or Peru, that the leaders did not simply tilt with the wind but actively pushed reforms through by logrolling unions, legislatures, and the courts. Because leadership is an idiosyncratic variable, its contribution to making reforms happen is hard to predict, but that does not diminish its importance.

In the end, *Bureaucrats* does pull together many variables that individually shed light on the probability of reform, among them the role of economic crisis in precipitating reforms, or the importance of having the governing party also control the legislature.[6] The report's main political conclusion, that SOE reform cannot be implemented successfully unless a country's leadership is convinced of its merits and committed to going forward, is valid and important, not the least because the World Bank has so often ignored this lesson in its own lending. But *Bureaucrats*' claim that "the framework and evidence presented in this chapter offer a basis for analyzing when and where SOE reform can succeed and be sustained" is unconvincing (p. 215).[7] The political desirability-feasibility-credibility model is purportedly confirmed in the sample of countries studied, but only because the model's (subjective) independent variables are self-rated by the authors to be consistent with the known outcomes. The reasoning is mostly circular, that is, in cases where reforms were successfully implemented, it is argued that they were politically desirable, feasible, and credible, and where they were not, the opposite is asserted to be the case.[8]

(a) *Political Cost-benefit Analysis*

Since the political analysis in *Bureaucrats* is static, it does not consider how the political costs and benefits of SOE reform are sequenced, nor the speed at which reforms are implemented. But speed and sequencing are important aspects of a country's reform strategy. Assuming for the moment that SOE reform is good economics, its political attractiveness should depend on the size and timing of the political costs and benefits. In the typical case, the political costs must be borne up-front, in the form of antagonizing labor unions, managers, suppliers, and other powerful beneficiaries of state ownership. In return, some political benefits may flow immediately (e.g., proceeds to the treasury, or income and wealth redistributed to one's supporters), while others will materialize in later years, in the form of better quality or greater supply for consumers, lower burdens on taxpayers, attractive returns to investors, higher exports for the country, and so on. The political attractiveness of SOE reform depends on the magnitude of these costs and benefits as well as their time distribution, their degree of unpredictability, the discount rate of political leaders, and leaders' attitude to risk. One could speak, as it were, of the expected net present *political* value of a reform, much like the traditional net present (economic) value of an investment. We do not know much, however, about how political costs and benefits relate to economic costs and benefits.

Nonetheless, a few propositions can be advanced. One is that privatization will be more attractive politically if the political benefits can be preponed and the political costs postponed. A second conclusion is that the more uncertain the benefits of reform, the less politically attractive it will be. This raises the question of how those uncertainties can be reduced. A third conclusion is that leaders with higher discount rates may find SOE reform less attractive than those with lower discount rates. Even if leaders' discount rates cannot be changed, it is useful to recognize that countries may differ in this respect and therefore may respond differently to similar reform opportunities.

Many of these ideas come together in thinking about the *speed* of reform, whether of SOEs or anything else. Shock therapy calls for all reforms to be done at once, as a result of which the political costs of reform peak in the early years, while the (uncertain) benefits are expected to flow in later years, making this a risky strategy for those in power. Such a risk may be worth taking only if the initial economic conditions are dire, as they were in many transitional economies after the collapse of Communism or in the highly indebted developing world in the 1980s. For instance, when Argentina plunged into hyperinflation in the late 1980s, policies designed to kill inflation were not merely politically feasible, they were in fact politically attractive. Moreover because privatization could help contain inflation by reducing the fiscal deficit and inflationary expectations, it promised *additional* and *immediate* macroeconomic benefits that apparently were sufficient to make the policy politically desirable even in the short run.[9] The longer term benefits that might have ensued at the firm level from the change in ownership were a bonus rather than a prerequisite for reform. The crisis environment also made the risks of reform more acceptable, since the consequences of inaction were demonstrably awful.[10] Similarly, in the transitional economies, quick privatization was seen as a way to make the political changes irreversible and therefore attractive in its own right (e.g., Boycko Shleifer and Vishny, 1994).[11]

The conclusion then is that speedy privatization is more attractive politically when initial conditions are dire. The deep privatizers in Table 3 were all mired in economic crisis when they embarked on privatization. Thus, economic crisis seems to be a necessary condition for swift privatization. But it appears not to be a sufficient condition, as shown by the absence of speedy privatization in countries like Brazil that faced macroeconomic crises at least as severe as those in Argentina or Peru. *Bureaucrats* describes the crisis in Ghana in 1983 as "arguably the worst in our sample," yet the country did not reform SOEs or privatize swiftly or deeply.[12] Conversely, countries such as Malaysia appear to have privatized quite deeply, even though they did *not* face a macroeconomic crisis similar to Argentina, the Philippines, or Peru.

Bureaucrats does not deal satisfactorily with these misfits (see Figure 1). It pays scant attention to countries such as Malaysia that privatized deeply in the absence of an economic crisis, and it explains away the slow pace of reform in crisis-ridden Ghana as being due entirely to the government's low credibility with private investors and SOE workers. Both types of misfit deserve more inquiry and explanation.

Non-crisis privatizers such as Malaysia represent the general case of slow or gradual reformers, an extreme example of which is China, which has reformed SOEs gradually but privatized very little (see Qi, 1989 and

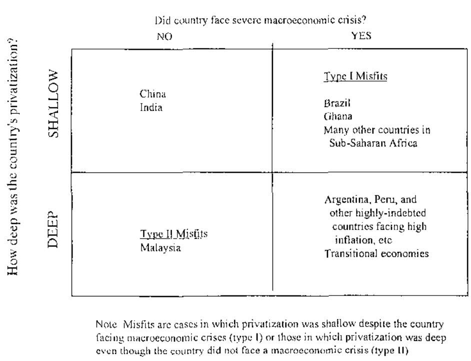

Figure 1. *The relationship between economic crisis and privatization.*

Boardman, 1995). Korea too falls into this category, even though *Bureaucrats* embraces it as a successful reformer and claims that the Korean experience is consistent with the political desirability-feasibility-credibility model (more on this later). *Bureaucrats* is right in identifying the critical role of macroeconomic crisis in precipitating SOE reform, and while that may be the only condition under which privatization is swift, it is not the only condition under which privatization is deep. It just so happens that the World Bank's policy lending occurs usually in the context of economic crises, and therefore the Bank understands the dynamics of crises-driven reforms better than those of non-crisis reforms. The World Bank's structural adjustment loans also have a short disbursement period, usually 1–2 years, which causes Bank staff to think in terms of quick and deep reforms rather than phased-out reforms. Yet, in cases such as Malaysia, SOE reform was deep despite being gradual. I believe the same will turn out to be the case in China.

It is not difficult to see why countries that are not in a crisis may want to reform gradually. Gradualism spreads out the political costs of privatization and allows the benefits of reform in one industry or one round of reforms to be reaped before costs are incurred in other rounds. By confirming that the anticipated benefits of reform are realized, or by demonstrating that the costs of reform were not as great as feared, it reduces uncertainties and thereby builds support for reform. Gradualism also allows for learning between rounds of reform. World Bank officials may feel that the learni ng that has been taking place in Washington DC. obviates the need for member countries to learn by doing, but governments may disagree. In the absence of a crisis, they may see no harm in taking the time to make sure that international experience is properly adapted to their national conditions.

On the other hand, gradualism carries the risk of degenerating into inaction. Governments can postpone all manner of reforms in the name of gradualism. But a general model of policy reform must consider the possibility that governments will differ in self-discipline and in their time horizon for policymaking. Not all governments in the developing world look only one or two years into the future, and not all of them consistently take the path of least resistance. *Bureaucrats* itself includes the example of Korea, which it regards as

> ... unique among the countries in the sample in that both the costs and benefits to the leadership and their constituencies of SOE reform were low...There was, for example, no regime change or coalition realignment during the period of analysis. Instead, slowing per capita GDP growth and increasing SOE losses *that might not have been considered serious problems in other countries were sufficient to make SOE reform politically desirable. ...The Korean government had a strong commitment to fiscal discipline, [and] rising SOE deficits, however small compared to the government's overall budget deficit, were at odds with this commitment* (p. 218, emphasis added).

Far-sighted government, or self-disciplined government, may sound like an oxymoron, but such cases do exist. At a minimum, one should entertain the possibility that governments will differ in their degree of self-discipline and the length of their planning horizon. More generally, one should consider the possibility that government failures can vary across countries, just as market failures vary across industries and countries. Moreover, surely the optimal SOE reform strategy must depend in part on the extent and nature of those government failures (Wolf, 1991). Where government failures are low, SOE reform *without* much privatization — at least without immediate and deep privatization — may not be bad transition strategy. One wishes *Bureaucrats* had considered these possibilities, and asked why government failures are higher in some countries than others, or what might be done to reduce those failures.

4. IS PRIVATIZATION GOOD ECONOMICS?

Up to this point we have assumed that privatization is good economics. The quote from *Bureaucrats* with which the paper began spoke of a "growing consensus that governments perform less well than the private sector in a host of activities." But does such a consensus in fact exist, and if so in what circles, and with respect to which activities?

Bureaucrats assumes that the consensus is quite broad — by no means limited to Washington DC. It also endorses privatization with relatively few qualifications. Besides recommending that privatization should be pursued only if a country is politically ready to do so, the only other important qualification is that in the case of monopolies, privatization must be accompanied by sound regulation. If a country is not politically ready, *Bureaucrats* offers several suggestions on how that readiness may be enhanced. All these possibilities, including alternative ways in which SOEs may be reformed, are summarized in a helpful decision-tree in the final chapter.

I believe policy makers in the average developing country are more skeptical than the authors of *Bureaucrats* about the promise of privatization, perhaps not in the abstract, but when applied to particular firms or industries in the unique conditions of their respective countries. They are far more skeptical about what the local private will be able to deliver, about their own ability to regulate privatized firms, and about how the benefits of privatization will be distributed across society. They are also more troubled than the World Bank about relying heavily on foreign capital and expertise, or on local minority ethnic groups, to make privatization a success (Chua, 1995). *Bureaucrats* does not concern itself with most of these issues, except for regulation. Its main concern is with the impact of privatization on efficiency and the government budget.

To make the case that privatization will improve efficiency, *Bureaucrats* begins by summarizing all that is wrong with SOEs. It shows that SOEs in developing countries have been money-losers, that they have sucked up credit in domestic markets, that their productivity is low, that they have depended heavily on government transfers, and that they are also terrible polluters. The reader will also learn that *if* subsidies to SOEs could be reduced by 5–10% by making them more efficient, the resources freed up could feed, clothe, or educate a lot of people. Policy makers from developing countries might agree completely with this analysis; perhaps that is why in the second half of the 1980s many countries cut back on fresh investments in SOEs (World Bank, 1995, p. 29). But a case *against* SOEs only goes some distance in making the case *for* privatization.

To make the positive case for privatization, *Bureaucrats* has to show that the performance of these SOEs would improve under the same market and national conditions. To make that case, *Bureaucrats* draws on three sources of evidence: its own 12-nation study of best practices; an earlier Bank-sponsored study of the welfare consequences of privatization (Galal *et al.*, 1994); and the general literature, including other studies produced by Bank staff (e.g., Levy and Spiller, 1996). The first of these studies evaluates SOE reforms at the country level, the second does so at the firm level, and the third consists of heterogeneous studies.

(a) *Bureaucrats' best-practices study*

The best practices study in *Bureaucrats* looked at the SOE reform strategies of nine developing countries that varied widely in size, income level, region, initial economic conditions, and success with SOE reform. Countries such as India or China that have resisted the World Bank's advice on privatization were included in the sample, as were countries that the Bank likes to hold up as examples of sensible reformers (e.g., Chile, Mexico). The study also used a broad definition of SOE reform, comprising of privatization, competition policy, hard budgets, financial sector reforms, and changes in the relationship between government and SOE managers. The study's aim was to identify which countries were more successful with which reforms and why. For this purpose, success was judged by the profitability, productivity, and the savings-investment gap of the country's SOE sector.

Even at the outset, this was a knotty research design. Performance measures such as the ones used tend to be affected by factors other than the reforms being implemented, giving rise to attribution problems. For instance, SOE profitability may be affected by exogenous factors like GDP growth rate or conditions in international markets. Another problem is that the small sample size makes it impossible to reach definitive conclusions about the effectiveness of different reforms, although it permits issues to be studied in greater depth in the selected cases. Finally, the impact of reforms at the firm or sector level cannot be gauged by changes in performance measures for the SOE sector as a whole. But these inherent difficulties are compounded by methodological flaws that reduce the value of the best-practices study.

The biggest problem has to do with how the success or failure of reforms is assessed. To begin with, two of the three success indicators used — financial profitability and the savings-investment gap — are poor surrogates for the efficiency of SOEs.[13] For instance, these indicators change when prices change or SOEs alter their rates of investment. Only the third indicator, SOE productivity, is relevant, but *Bureaucrats* uses some undefined combination of all three indicators to rate countries' reform effectiveness. More seriously, *Bureaucrats* looks not only at the change in the pre- and post-reform values of the chosen indicators, but also at their absolute value at the end of the reform period. But only the change in the indicators is relevant for assessing the effectiveness of reforms. Even the labeling of countries reflects this error in methodology: the most successful reformers are labeled "better performers" rather than "most improved performers." Not surprisingly, the three countries receiving the highest rating — Chile, Korea, and Mexico — are among the richest countries in the sample, and their SOEs were performing better than the SOEs of the other countries even before reforms were implemented.[14] If *changes* in productivity alone had been considered, India and Turkey would have moved from the lowest category of performance to the highest, and Chile would have moved from the highest to the lowest. Although the report does not put it this way, the methodology used leads to the absurd conclusion that SOEs in poor countries could have performed better had they been located in richer countries![3]

The third problem is that privatized firms are included in the pre-reform set of SOEs but not in the post-reform set. In countries where many firms were divested as part of the reform program, the set of post-reform SOEs could be significantly smaller in size than the pre-reform set, which makes it impossible to judge the effectiveness of privatization or any other reform. Despite these flaws, *Bureaucrats* somehow arrives at the following kinds of conclusions:

> ...although it is difficult to attach specific weights to the relative importance of these components [of SOE reform], divestiture appears to be critical to success, especially where the initial size of the SOE sector is much larger than the world average of about 10% of GDP. (p. 55).

> ...although difficult to establish concretely, it appears that a reduction in the SOE share in the sample is strongly correlated with improved performance for the enterprises that continue to be state-owned. (p. 70).

One can only surmise that conclusions like these are the authors' axiomatic beliefs, couched as scientific findings.

(b) *The case of small, poor countries*

One wishes *Bureaucrats* had made a strong and convincing case for why privatization is an economically sound idea in low-income countries. Instead, it takes pot shots at the poor performance of SOEs in these countries, while hiding behind the success stories of privatization in middle-income countries.

The report mentions more than once that the SOE sector is larger and has performed worse in low-income countries than in middle-income countries. Poor countries, it is argued, can least afford the inefficiency of SOEs and ought therefore to privatize vigorously. Yet, with the exception of Ghana, low-income countries in Table 3 appear to have privatized only a tenth or less of their SOE assets. Even in the case of Ghana, three-fourths of the priva tization proceeds came from one transaction, the sale of 27.5% of the equity in Ashanti Gold Mines, without which Ghana too would have privatized only a tenth of its SOE sector. Why have not these countries privatized more?

Bureaucrats explains it all as the result of political obstacles, i.e. reform was either politically undesirable or infeasible, or the government's efforts were not credible. These factors probably played an important part, although one would have thought that these countries were politically ripe for reform. For instance, in the 1980s, macroeconomic performance in much of Africa was "catastrophic..[on] almost every conceivable yardstick" (Callaghy and Wilson, 1988, p. 182).[16] Moreover, power was often concentrated in the hands of national leaders, who enjoyed surprisingly long tenures in many countries. If, despite these conditions, SOE reform was not politically desirable or feasible, is it possible that other nonpolitical factors may have been the binding constraints?

One oft-mentioned obstacle is the underdeveloped status of market-supporting institutions in low-income countries. The *Bureaucrats* sample includes several countries with per capita income below US$600. Of these, the larger countries, such as China and India, have relatively well-developed capital markets, vibrant private sectors, and competent bureaucracies, but their smaller counterparts, such as Ghana, Nigeria, or Senegal, are weak on all these fronts. Ariyo and Jerome note in their article in this issue that the preconditions for privatization have generally been lacking in the poor countries of Africa. SOE ref orm has often meant closing down and liquidating SOEs rather than revitalizing them through privatization.[17] Local buyers have lacked money and expertise. SOEs have therefore been bought on deferred payment terms or with loans from state-owned banks that have not been serviced properly after privatization. In addition, governments have had to extend protections and subsidies to entice buyers or to keep privatized firms alive. Also disturbing has been the very heavy reliance on foreigners or non-resident nationals at every stage of privatization, from providing technical advice, to selecting firms for divestiture, restructuring them, valuing them, and investing in them. A senior World Bank official regarded limits on foreign dependence as a "principal reason why privatization is proceeding so slowly in several African countries" (Dia, 1992), p. 5. Even when African countries have opened their doors to foreign investment, the response of investors has been often been lukewarm at best.

For these kinds of reasons, one is hard pressed to find success stories of privatization in Africa, comparable to those in Asia or Latin America. For a while, Ghana promised to be that showcase, but after 10 years of continual structural adjustment and reforms, those hopes have been dashed. While Ghana's progress has been impressive on some fronts, it has not been particularly successful in reforming its SOEs (Herbst, 1993, pp. 98–100). More than 10 years after beginning SOE reforms, the country adopted in 1995 the Accelerated Privatization Program whose goal was to divest 200 firms quickly, but by 1998 only than a quarter of that number had been sold. More recently, Zambia has become the Bank's favorite reformer in sub-Saharan Africa, but the sustainability of that country's reforms remains to be seen.[18] How can privatization gain momentum in Africa without successful examples of its use in the region? Worse, how can it gain followers when countries that have tried it have had consistently disappointing results.

Privatization cannot gain momentum until a cross-section of national opinion leaders is convinced that it will work in the local context. That, in turn, has to grow out a country's local experience with privatization or with demonstrable successes in neighboring countries. I doubt that officials in sub-Saharan Africa will be sold on privatization just because it seems to have worked well in Argentina or Malaysia.

Perhaps the role of the state, as reflected in public ownership, has to be bigger in poorer countries than in richer countries. History has shown that everywhere governments have taken the lead in the early stages of economic development (Gerschenkron, 1962). The term developing countries includes nations of widely divergent living standards. The per capita income of upper-middle-income developing countries is 10 times that of low-income developing countries. (On the other hand, the per capita income of the average industrialized country is only six times that of the upper-middle-income developing country.) If SOEs account for 8–10%, of GDP in upper-middle-income and industrialized countries, is the 15% share for SOEs in low-income countries outrageously high?[19] With 85% of the economy in private hands, low-income mixed-economies are already predominantly private. The sad reality in low-income countries is that weak government is matched by equally weak markets. Privatization not only moves assets from the public to private sectors, it often also moves them from the formal to the informal sector, because much private activity is deliberately kept outside the vision of the state, which is seen "as hostile to their economic welfare" (Barad, 1994), p. 192. Until public and private institutions are strengthened, pressing for rapid privatization may be barking up the wrong tree. At any rate, the unique problems of low-income countries cannot be solved solely with remedies borrowed from richer countries. Agencies such as the World Bank should scour these countries for local innovations that seem to have worked well and encourage other poor countries to adopt them. Examples that come to mind include the microlending enterprise pioneered in Bangladesh (Grameen Bank), or the town and village enterprise pioneered in China (more on this later). But so long as the World Bank thinks only in terms of Western models and solutions, it risks overlooking indigenous innovations.

(c) *The case of monopolies*

I will turn next to the question of how the promise of privatization varies across industries with differing economic characteristics. *Bureaucrats* is right to argue that "in competitive markets the literature gives the edge [in efficiency] to the private sector [over the public sector]" on both theoretical and empirical grounds (p. 37). But SOEs in competitive markets make up only a small portion of the SOE sector in developing countries. To be sure, there are still the state-owned casinos in Ghana, the cookie factories in Egypt, the watch companies in India, and the salt mines in Mexico; many such firms can, should, and have been, privatized in the last few years. Because of their small size however they account for only a small share of SOE assets.

In most countries, the SOE sector consists mainly of firms operating in four sectors: public utilities, heavy industries, financial services, and extractive industries. These firms tend to be large and monopolistic or oligopolistic. They all entail either high *risks* or present opportunities to earn high *rents*. Neither the theoretical nor the empirical literature suggests unambiguously that such firms will perform better if privatized. *Bureaucrats* relies heavily on one study to show that privatizing such firms may be economically desirable (Galal *et al*., 1994).

That study, funded by the World Bank, calculated the results of privatization in a sample consisting of four telephone and electricity monopolies, four airlines, a port, a trucking firm, a lottery company, and an electricity generation company. The firms were based in Chile, Malaysia, Mexico, and the United Kingdom. The most publicized finding of this study was that in 11 of the 12 cases, global welfare increased as a result of privatization, after controlling for non-ownership factors as judiciously as possible. What is more, the study found that privatization usually made winners of all groups, including government, investors, customers, and even workers. Moreover, the study found that this happy result held true even when monopolies were privatized, not just in industrialized Britain, but in the other countries as well. Finally, the study showed that the welfare gains from privatization for both foreign and domestic groups were often substantial. The study made a spl ash when it was released, and provided a shot in the arm for privatization advocates.[20]

The study had its limitations, however, many of which the authors point out in their lengthy book, even if others have chosen to forget them.[21] First, the sample used was not random but handpicked in consultation with the governments involved. Therefore it may have been skewed toward successful privatizations. Second, the sample consists of firms from one rich country and three upper-middle-income countries, which raises once again with the question of how relevant the findings are for lower-middle and low-income countries.[22] Third, the sample includes firms from only some of the sectors that SOEs dominate, e.g., airlines and telephones, but none from other sectors in which they participate widely, e.g., roads, railroads, water, sewerage, banking, and natural resources. Therefore, pending further research, the findings should not be assumed to hold for all infrastructure or monopolistic sectors. It should also be remembered that the study projected the long-term outcomes of privatization based on the actual outcomes for the first few years after privatization. It remains to be seen if the short-term gains will be sustained. One reason for skepticism is that nationalization also produced short-run improvements in output and productivity that turned out to be unsustainable.[23] Finally, the authors do not adjust for income distribution effects or price distortions in their measures of welfare; the use of the word "welfare" in the book's title is therefore a bit misleading.

These are hardly fatal limitations, though. Many middle-income countries have not privatized very much (e.g., Colombia, Ecuador, South Africa, Turkey), and the sectors studied in Galal *et al.*, are very important in most countries. My only point is that *Bureaucrats* ought not to have extended blithely the study's findings beyond the settings in which they emerged. Almost all of the evidence in *Bureaucrats* showing that regulatory contracts with private firms are superior to performance contracts with SOEs comes from the telecommunications industry (e.g., Levy and Spiller, 1996; Galal and Nauriyal, 1995). The discussion pertaining to telecommunications is excellent, but the transferability of that experience to other monopolistic industries is assumed rather than demonstrated.

Telecommunications is uniquely qualified to yield long-run gains from privatization and deregulation (see Ramamurti, 1996, pp. 21–34). Its growth potential and cash flow patterns are usually outstanding, because pent up demand is large and consumers are willing to pay high enough prices to allow producers to recover their investment in 2–3 years. Regulatory problems are mitigated by competition, which is strengthened each day by technological change. Externalities are relatively unimportant and can be accommodated through light regulation and minimal subsidies (see Table 4 for a comparison of telecommunications and other infrastructure sectors). The regulatory task is manageable even in the long run, and even in countries lacking regulatory experience and institutions.

Sectors such as railroads, however, are harder to regulate after privatization (see Ramamurti, 1997). The regulatory task can be especially difficult in sectors such as highways or water and sewerage, where competition is weak or totally absent, investments are lumpier, externalities are much more important, and payback periods run 8–10 years or more, thereby increasing uncertainty and risk for all contracting parties. Renegotiation is likely to be the rule, brought on by unanticipated developments or simply opportunism on the part of investors and governments. History is full of examples in which such agreements have fallen apart a few years after they were signed (for a good overview, see Wells and Gleason, 1995). It is a safe bet that the recent Asian crisis will cause agreements negotiated only a few years back in that part of the world in infrastructure sectors to unravel. In Mexico, the $5 billion private investment program in roads fell apart after that country's currency crisis and left the government holding most of the debt involved (Wright, 1997).

The point is not that privatization is undesirable in sectors such as roads and water, but that its promise is much more dubious in these sectors. Therefore, privatization schemes need to be drawn up much more carefully than in the case of telecommunications, where one can take the attitude that even a badly done privatization is better than the status quo (a viewpoint often heard in the World Bank). In sectors such as roads or water the Bank should not be in hurry to spread the privatization gospel. It is prudent to proceed in a deliberate manner, with at least one eye on the rearview mirror.

5. WILL BUREAUCRATS EVER GET OUT OF BUSINESS?

Bureaucrats in Business was a catchy title for the World Bank's report. In just three words it pointed out the absurdity of the status quo, because the images evoked by "bureaucrat" conflict with those evoked by "business." Yet, reality is more complicated, and bureaucrats will,

Table 4. *Differing characteristics of infrastructure sectors*

Sector	Growth potential	Positive cash-flow potential	Competitive and regulatory risks	Externalities and need for subsidies
Telecommunications	High	High; short payback period	Moderate competitive and regulatory risks	Subsidies necessary only for achieving universal service goals is rural areas
Roads	Medium	Low; long payback periods	High regulatory risks due to uncertain costs and demand, and heavyhanded regulation likely when competition from alternatives is weak	High externalities; subsidies may be necessary to keep tariffs low
Railroads	Low	Medium; often little new investment required, and existing assets usually leased at low rates rather than sold outright	Regulatory risks lower if competition exists from substitutes, which depends on level of development of alternative modes of transport	High, because of contribution to hinterland development, and congestion issue in the case of urban transportation
Water/sewerage	Medium	Low, because large up-front investments necessary, and consumer's ability to pay is poor	High regulatory risks due to obsolescing bargain problem and essential nature of water; Competition potential low	High, due to essential nature of product, and health/safety considerations

and should, play at least four crucial roles in business in the years to come.

The authors of *Bureaucrats* are too sophisticated not to have realized that three types of individuals come together in the running of SOEs: enterprise managers, civil servants, and politicians. "Bureaucrats" usually refers only to civil servants and not to the other two groups. Indeed, most SOE managers would be offended if they were called bureaucrats. In the discussion that follows, however, like the authors of *Bureaucrats*, I will use "bureaucrat" to mean civil servants, politicians, and managers.

The first and most obvious role of bureaucrats is in the running of businesses till such time that all SOEs are privatized. This role may be regarded as transitory, but the evidence of the last decade is that the transitory phase can last one or two decades, not just one or two years, even in mixed economies, and even when a country's leaders are zealous privatizers (e.g., Czech Republic or Russia). It follows therefore that the capacity of governments to manage SOEs must continue to be strengthened, rather than ignored on the presumption that the transition period will be short. Unfortunately, much of the academic community, and international agencies like the World Bank, have given up on this objective.[24]

China's experience offers several interesting ideas for reform within the public sector, but these are not given much consideration in *Bureaucrats*. A particularly important example is the case of the town and village enterprise (TVE), which are controlled by local officials, whose CEOs serve at the pleasure of local leaders, and whose profits go to the town or village. Despite this kind of public control, TVEs are aggressive competitors, have grown rapidly, are efficient, and have formed joint ventures with foreign investors and Chinese SOEs (Naughton, 1994). *Bureaucrats* dismisses the success of TVEs as due to the fact they face hard budgets and operate in competitive markets, and there is no explanation for why community or public ownership has not hampered their performance. The important question for other countries is whether public ownership works more effectively when there is competition or accountability is decentralized to the local level rather than centralized at the federal or provincial level. Might other countries profitably copy this institutional form in preference to both private ownership and federal government ownership, and if yes, under what circumstances? Might the TVE idea be particularly valuable in low-income countries, e.g., sub-Saharan Africa, or is it somehow limited by conditions unique to China?

Unfortunately, *Bureaucrats* dismisses innovations such as the TVE much too quickly, maybe because they complicate its simple story about how bureaucrats cannot be good at business. Similarly, it rejects the value of performance contracts between governments and SOEs, going so far as to say that they can do more harm than good, even though Korea seems to have had much more success with such contracts than other developing countries. It also does not ask if partial privatization, which is politically more palatable than full privatization, can improve a firm's performance. Two of the three Malaysian cases studied in Galal *et al.* (1994) involved partial privatization, and the positive results in those cases appear to have matched the results obtained from full privatizations in other countries. Should not we try to learn all we can about these hybrid forms of organization, and about the conditions under which they may offer positive results? Can these partial forms of privatization help reduce government failures without imposing the political costs of outright privatization?

The second role of bureaucrats is devising and implementing strategies for SOE reform. Although *Bureaucrats* recognizes that SOE reform has many dimensions, it does not pay much at tention to the sequencing of reforms, nor therefore does it consider the merits of alternative reform paths. The message one picks up from *Bureaucrats* is that outright and immediate privatization, supported by pro-competition policies or sound regulation (when competition is infeasible), is the best option in every case. Other reforms, such as management contracts, hard budgets, or performance contracts with SOEs, are regarded as second-best solutions to be used only when outright privatization is not feasible. Even if these prescriptions are sound, we have seen that most countries are unable or unwilling to implement big-bang reforms. Therefore, we would benefit from a better understanding of the implications of alternative reform paths. What are the implications, for instance, of liberalizing and deregulating first and privatizing later, or of privatizing banks first and non-bank SOEs later or vice versa?

In practice, countries such as China and India have liberalized and deregulated their economies significantly, but without privatizing very much. Others, such as Argentina and Chile, have liberalized, deregulated, and privatized, all at once.[25] The overwhelming pattern in Latin America has been to privatize control, not just ownership, while in East Asia, the more common pattern has been to divest a minority of the shares, with governments retaining control. Some countries have preferred to sell SOEs to strategic investors, while others have opted to sell to dispersed investors. Likewise, some countries have restructured their SOEs extensively before privatization, while others have left restructuring to the new owners. Countries have also targeted different types of buyers, ranging from employees and managers, to local business groups and foreign multinationals.

Countries have also differed in the goals of reform. Whereas *Bureaucrats* assumes that there is only goal of reform, namely, to improve efficiency, countries also worry about other goals, including the distribution of income and wealth, national sovereignty, or the competitiveness of national firms. According to Nolan and Xiaoqiang's article in this issue, China's reform of large SOEs is designed to transform them into world-class firms that someday can hold their own against their multinational rivals, while still being Chinese-owned. Selling SOEs immediately to foreign multinationals would not have allowed this objective to be achieved. Similarly, privatization can be used to strengthen a country's large business groups, as it was in Argentina, albeit unintentionally. The point is that once SOE reform is seen as a sequential process spread over many years and motivated by many goals, it presents complex strategic choices. Who but bureaucrats will be responsible for making those choices?

The third role of bureaucrats in business is in the regulation of privatized firms. Most large-scale privatizations are public-private arrangements in which the government has relinquished responsibility for *production*, but is still responsible for *financing* or *regulation*, because so many SOEs operate in imperfectly competitive markets, or generate externalities, or produce merit goods (Ramamurti, 1997). In some cases, governments own golden shares or hold seats on the board of privatized firms. In other cases, they must renegotiate concession or license agreements as unanticipated contingencies arise or economic conditions change. In addition, governments have ultimate responsibility for firms that are too large or too important to be allowed to fail, like banks (witness the aid extended to Mexican banks after the 1994 peso crash). Except in the case of privatized firms operating in highly competitive markets, bureaucrats will have to regulate privatized businesses for the fores eeable future.

The fourth role of bureaucrats in business is perhaps the most difficult of all. It involves building the institutions that underpin any well-functioning market economy, including the legal system, property rights, capital markets, and regulatory institutions. Despite the opportunity to learn from advanced countries in these areas, the development of these institutions occurs slowly, because matters like credibility, reputation, tradition, attitudes, and skills, are not created overnight, as many transitional economies have discovered to their dismay. Despite all its flaws, government is the principal means by which societies can create these institutions. As Sen and Dreze (1995) have noted, "The nurturing of an early market mechanism by an active state does not, of course, preclude a more self-sufficient role of the market *later on*" (p. 19; emphasis in original).[26]

Therefore, bureaucrats will not get out of business completely, not even when everything governments own has been privatized. This means that we must continue to search for ways to make governments more effective in their various business roles, even as we search for ways to make markets more effective. Being market-friendly does not have to mean being government-*un*friendly. The World Bank itself is a bureaucracy — and one owned by governments to boot — that dabbles in member countries' businesses all the time. Its private sector arm, the International Finance Corporation, is actively engaged in starting up and supervising businesses in developing countries. Few would dispute the overall positive contribution that "bureaucrats" in these international organizations have made to the development of industry and commerce in the developing world.

6. CONCLUSION

If this critique has emphasized the limits of privatization it is only because *Bureaucrats* has overstated its promise. There is much in *Bureaucrats* with which I agree, especially in the chapter on contracts, which proposes a unified way to think about management contracts, performance contracts, and regulatory contracts. In this article I have focused on the areas of disagreement, of which there are clearly many.

Fundamentally, I share the Bank's belief that privatization is a powerful and positive idea, and the World Bank deserves credit for the international diffusion of that idea. But the limits of that idea when applied to particular markets or countries must also be recognized. As new evidence comes in those limits should be reviewed. As of now, the efficacy of privatization in low-income countries has yet to be established convincingly, and even in middle-income countries, the jury is still out on the long-term results of privatization in industries characterized by externalities, long payback periods, subsidies, and messy regulation (roads, ports, water, etc.). There are many signs that privatization and deregulation are yielding very positive results in sectors like telecommunications, but whether similar results will ensue in other sectors, through good and bad economic times, remains to be seen.

The speed at which SOE reforms are carried out is another issue that merits further analysis. The notion that faster is better may be true for countries in deep economic crisis, but gradual reform may be a more realistic and preferable choice in other cases. In the context of SOE reform, this means understanding more fully the implications of alternative reform strategies. Our models of the reform process must also allow for the possibility that government failures are less serious in some countries than others. We must also search for ways to reduce those failures in all countries, because, like it or not, bureaucrats will influence business outcomes for a long time to come.

NOTES

1. The method used comes reasonably close to separating deep privatizers from shallow privatizers, except in cases such as Chile, where our procedure yields a very low privatization percentage (6%) while country studies put the percentage at closer to 60% (see Luders, forthcoming). The reason for this large discrepancy is unclear; possibly our procedure overvalues the market worth of companies such as Codelco, the large Chilean copper company. The estimate for Philippines may be distorted if the share of SOEs in GDP, obtained from the statistical appendix in *Bureaucrats,* did not include assets belonging to the Asset Privatization Trust. Alexander and Corti (1993) estimate that two-thirds of the SOE assets had been privatized in Argentina, while our estimate is much lower at 48%. Our estimate for Peru is consistent with the assessment in Kuczynski, forthcoming of what remains to be privatized in that country.

2. Data on privatization in transition economies do not include the assets of thousands of small and many medium enterprises that were auctioned to employees or managers. Since such firms may have accounted for a third or more of total SOE assets, their omission is material.

3. World Bank (1996), p. 53 estimates that in December 1995, 40% of the SOE assets in the Czech Republic were still in state hands, but this ignores the privatized assets owned indirectly by the government through state-owned mutual funds. See also Regan and Hayes (1994) for a review of the difficulties of mass privatization in the Czech Republic.

4. This is no small accomplishment, given the thousands of enterprises involved and their aggregate importance in the economy.

5. I am referring here to the developing world as a whole. In individual countries, privatization is at different points of the S-curve, having crossed the take-off point in some (e.g., Argentina), being at the take-off point in others (e.g., Brazil), and a long way from the take-off point in still others (e.g., China or India).

6. Specifically, the model incorporates the following variables: to estimate the desirability of reform, it considers whether there has been a regime change, a coalition shift, or an economic crisis, and it identifies the support base of government decision makers. To judge reform feasibility, it takes into account such characterist ics as the constitutional or procedural requirements that make reform more or less feasible, and the distribution of political power among various entitites of government. For credibility, it relies on such indicators as reputation assessments by investor risk services, the design of the reform, and the constraints on executive discretion. In a more controversial vein, *Bureaucrats* claims that these indicators can be used to predict the likelihood of reform because they are "objective characteristics that can be observed independent of the reform attempts and often measured with quantitative indicators." (p. 216).

7. It is not fair, of course, to expect *Bureaucrats* to explain fully and persuasively why some countries reformed their SOEs and others did not, when political scientists have struggled with such questions for years without much success.

8. One particularly interesting example is the case of Korea. *Bureaucrats* argues that reform was politically desirable there even though both the benefits and costs were low, because the benefits exceeded the costs. The reader never finds out how the authors arrived at this conclusion.

9. Bruno (1996) provides an excellent summary of the literature on the relationship between macroeconomic crises and countries' proclivity to pursue economic reforms.

10. This relates to the saying that things often cannot get better until they get wo rse.

11. Boycko, Shleifer, and Vishny (1995) have argued this very strongly in the Russian context, and the same consideration influenced the pace of privatization in the Czech Republic.

12. Ghana's relatively high ranking in Table 3 results largely from the privatization of one company, Ashanti Gold Mines, which in 1994 fetched the government US$454 million, or fully three-quarters of the total proceeds from privatization from 1988–95.

13. Financial performance is measured by net operating surplus as a percentage of sales, and by profits before taxes as a percentage of sales. The savings-investment gap is measured by the extent to which SOEs rely on outside sources to finance their operations, expansion, and debt service, and is expressed as a percentage of GDP.

14. Their average per capita income in 1990 was US$3276, compared to US$573 for the mixed performers and US$896 for the poor performers.

15. In a similar vein, the section on financial sector development finds that "the most successful state enterprise reformers in our sample had the highest levels of financial sector development" (World Bank, 1995), Figure 2.6, p. 89.

16. For much of the continent, output per head was lower than it had been in 1960. During 1980–84, the gross domestic product (GDP) of African countries declined an average of 1.4% a year, per capita gross national product an average of 4.4% annually, export volume 7.4%, and import volume 5.9% (Callaghy and Wilson, 1988 182 p.).

17. Referring to Ghana, Herbst (1993), p. 99, says: "It is doubtful that many of the companies the government most wants to sell are viable. The SOEs the Rawlings government initially singled out for privatization owed millions of dollars in back taxes and contributions to unfunded pension schemes; their physical plants were run down, and many had almost no managerial capacity. In the end, it is likely that many of these companies will have to shut down and their assets sold for scrap."

18. See White and Bhatia (1998) which holds up Zambia as having the most successful privatization program within its sample of ten African countries (p. 111). Referring to the changing attitude of African governments toward privatization, the study claims that "it is no longer a question of whether or not — or what — to privatize; it his how and when to privatize" (p. 1). Only time will tell if this assessment is correct.

19. The per capita income of low-income countries is one-sixth that of middle-income countries and one-fiftieth that of industrialized countries (World Bank, 1994), Table 1.

20. The results of this study were presented at a World Bank conference in 1992 and received a lengthy write-up in *The Economist* (June 13, 1992), pp. 73–14. See also Galal and Shirley (1994).

21. Limitations of the study are covered in Chapter 23 of Galal *et al.* (1994), especially pp. 534–536.

22. According to the World Bank (1997), all three countries are upper-middle-income countries. Their per capita incomes in 1995 were: Chile, US$ 4160; Mexico, US$3320; and Malaysia, US$ 3890.

23. To put it differently, the Galal *et al.* (1994) methodology might well have arrived at the conclusion that nationalization works, had it compared the performance of firms/sectors shortly before and after nationalization in the 1950s and 1960s. Even the Communist bloc countries registered impressive growth in output and productivity in the first two decades after switching to central planning.

24. Indicative of this situation, a search of the Uncover database of scholarly publications yielded over 1000 hits under "privatization" and less than 50 under "state-owned enterprise"!

25. To be sure, in sectors like telecommunications, competition was restricted for several years after privatization (see, for instance, Ramamurti, 1996).

26. The 1997 theme of the World Bank's *World Development Report* (World Bank, 1997) recognized the critical role that governments must play in the development process.

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