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UPP

UNDERSTANDING PRIVATIZATION POLICY: POLITICAL ECONOMY AND WELFARE EFFECTS

INSTRUMENT: SPECIFIC TARGETED RESEARCH PROJECT

THEMATIC PRIORITY: PRIORITY 7 "Citizen and governance in a Knowledge-based society"

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1.1 Introduction

Privatization is one of the main events of the economic history of the last decades, a landmark economic policy of the last two decades: its record to date is impressive, both in developed and developing economies. Yet some countries have pursued a consistent and sustained privatization policy as a part of wider reform packages, while in others ambitious programmes have been blocked on their way by adverse interest groups, so that privatization has been sporadic and small-scaled. Furthermore, some governments, have typically transferred the majority of capital of State-owned enterprises (SOE) to private investors, while in continental Europe the prevailing corporate governance model in privatised firms appears to be the separation of ownership and control, typified by government wielding power through pyramiding and statutory constraints especially in services of general interest (henceforth SGI). Finally, a cosmic "disconnect" is arising between the academic consensus and how privatization is perceived by the population, especially in transition economies and in the poorer regions of the world.

In these circumstances, it is imperative to analyse the true record of privatization and understand the causes behind failures in order to improve the process in the future. Despite the relevance of the process and the extensive research recently carried out, several aspects of privatization such as its determinants, methods, and economic and social implications warrant a systematic analysis and research efforts.

Against this background, the main objectives of the Project "Privatization Policy: Political Economy and Welfare Effects are: 1) to study the political and institutional incentives and constraints affecting privatization; 2) to analyse the interactions between private and public ownership and control of firms; 3) to evaluate the welfare effect of privatization policies on consumers, taxpayers and shareholders; 4) to identify the most appropriate policies to make privatization deliver the most desirable outcomes.

The Project adopts a multidisciplinary approach, mobilising researchers from economics, finance, political science, and judicial disciplines working in five universities and three research institutions of five European countries, including a new accession country.

1.2 Partners list

n°	Name	Acronym
1	Fondazione Eni Enrico Mattei	FEEM
2	Universitat Pompeu Fabra	UPF
3	University of Milan	UMIL
4	Universiteit van Amsterdam	UvA-CIFRA
5	IFO Institute for Economic Research at the University of Munich	IFO
6	Stiftung Wissenschaft und Politik - Deutsches Institut für Internationale Politik und Sicherheit	SWP
8	Center for Economic Research and Graduated Education, Charles University	CERGE-EI
9	University of Padua	UNIPD

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1.3 Project objectives

The UPP Project's first objective is to **study the political and institutional incentives and constraints affecting privatization**. More particularly, the Project aims to develop:

- a sound theoretical foundation for the link between electoral rules (i.e. majoritarian vs. proportional systems), political orientation and privatization activity;
- two international databases assembled jointly by economists and political scientists on political and institutional variables;
- empirical tests of the theoretical results using the original databases described above;
- studies of the political economy of privatization and regulatory reform covering the evolution, the sectoral breakdown and the methods of privatization processes also in Euro-Mediterranean Partnership countries.

The Project's second objective is to **analyse the complex interactions between private and public ownership and control** of firms, with special reference to regulated markets and SGI. More particularly, the Project aims to develop:

- a theoretical framework to evaluate the trade-offs between private and public ownership and control of corporations, and identify (if any) the optimal government's stake in models encompassing issues of regulatory governance;
- two datasets assembled jointly by economists and legal scholars with company ownership and performance variables and information on "golden share" provisions for OECD countries and for the Czech republic;
- empirical analyses on the evolution of ownership and control structures of privatised firms assessing the long term effect of changes of ownership structure on firm value in OECD economies and in the Czech Republic;
- empirical analyses on the different patterns of ownership and control as compared with the level of divesting government (central, intermediate, local), with special reference to utilities and public services, and taking into account also legal and statutory constraints embodied in the so called "golden share provisions".

The Project's third objective is to **evaluate the welfare effect of privatization policies** on several stakeholders, such as:

- consumers, analyzing empirically the impact of privatization, liberalisation and regulation of public utilities on individual and household welfare under different policy regimes, with special reference to SGI such as water supply, gas, electricity and telecommunications;
- taxpayers, studying the role of privatization in stabilizing the current budget and in

maintaining fiscal balance in the long-run both at the local and central level;

- shareholders, evaluating the stock market performance of European listed privatised firms in order identify the risk and return characteristic of this particular investment;

- employees, analyzing the long term effect of privatization on employment levels and wages in selected European countries.

The Project's fourth and final objective is to draw from the research milestones and from the results of a comprehensive ad hoc survey a set **of concrete policy recommendations** in order to make privatization deliver the most desirable outcomes. These recommendations will be strongly based on economic rationales taking into account the actual legislative and regulatory framework and the political and institutional constraints facing policymaking. They will be published in a policy report that will be presented at the final conference in Brussels in 2008.

1.4 Work performed

Summarizing the whole project period, we can say that all the activities have been completed in order to comply with the objectives as planned in the Description of Work (DoW). Overall, the implementation of the project by each workpackage (WP) fitted with the time line of activities and the deliverables have been accomplished according to the planned agenda. Each research study brought important results and most of them have been presented during the final UPP conference organized in Milan at the end of June 2008.

All UPP partners were involved in the preliminary activities necessary to develop the project action, such as the participation in the **Kick-off meeting** and the **Intermediate meeting** held in Barcelona and in Prague respectively. These activities were undertaken within **WP1**. The organisation of the meetings allowed to establish sound links among the consortium participants and to define some preliminary aspects of the work plan. On the other side, the organization of the **Final Policy Informing Conference** in Milan aimed at disseminating project findings and produced papers.

Beyond the normal co-ordination activities and management work under WP1, major efforts have been devoted in the implementation of **WP11**: dissemination of the Project's results was achieved using conventional outlets such as these workshops and conferences but the most important instrument was an ad hoc website.

The establishment of a dedicated website (http://www.uppproject.net) contributed to share information and project related material among partners. Particularly relevant to this aim was the realization of an ad hoc section for UPP in the portal entitled "Privatization Barometer" (PB), the major dissemination instrument of the project. Substantial network effects have been obtained in the dissemination activity of the Project's activities by leveraging on the high visibility of PB. As the access statistics show, most of present PB content is widely accessed and downloaded to be utilized as a fundamental research tool. The section of PB dedicated to UPP is targeting a wide audience, providing information on UPP progress in a widely accessible and non-technical language. The UPP section also displays scientific contents, publishing all project findings and mid-term scientific reports online. Moreover, the website tool established links with the web sites of the partner institutions to enhance the Project visibility.

A dedicated UPP Intranet section has been established and maintained, allowing to share information and project related material among partners in the restricted area, and to disseminate project information to a wider audience in the public space. It includes: (i) scientific contents; (ii) publishing all project findings and final scientific outputs; (iii) and to establish links with the partner institutions.

Another important means of dissemination under WP11 the issues of UPP Electronic Newsletter distributed every six months. The newsletters were disseminated through the existing PB newsletters mailing list on privatization-related issues, a wide list of academics, policy-makers and interested public at large. The first newsletter aimed to inform a wide audience about the project start and its main objectives while the following half-yearly reports provided updates on the work agenda. The last one, divulgated after the final conference, presented some important thematic and conclusions which were presented during that event.

Within **WP2** (Political determinants of privatization policies) the work team led by UPF completed their research projects fulfilling the terms of delivery as they were planned at the beginning. Workpackage 2 aims at explaining the observed differences in privatization outcomes across countries political determinants of privatization. For that end, it has worked simultaneously on several fronts. First, it established the guidelines for data collection, theoretical analysis, and empirical testing to analyse the role of institutions on privatization and the impact of privatization on political outcomes. Secondly, it collected data on variables characterizing political institutions and political orientation of governments. Thirdly, it built a theoretical framework for the analysis of voting behaviour and institutions, which provided testing hypothesis of the links between different aspects of privatization and the characteristics of political institutions. Finally, it empirically tested some of the theoretical prediction using the assembled database. The overall research work developed three important papers during the second reporting period which have been submitted as scheduled.

Under **WP3** (Privatization in the MEDA region) the work team led by FEEM has met with success the workpackage objectives. The research work on MEDA countries produced a survey of different aspects of privatization in that area. Two initial reports produced significant outcomes: a first report examining the water organizational framework in MEDA countries and the development of private sector participation in the context of urban water crisis has been completed and delivered in January 2007; a second Report completed and delivered in February 2007 analysed privatization as an element of the more general process of liberalization or movement toward the market as a regulator of human interaction in society. The efforts devoted to data collection in the area, including two fact-finding missions in Tunisia and Egypt, produced a brand new database reporting systematic information on privatization operations in the MEDA countries which was completed in July 2007 with a significant advance on the agenda. Other two papers have been produced during the second reporting period: the first one was an attempt to assess the progress of the privatization process in the MEDA countries of Algeria, Egypt, Israel, Jordan, Lebanon, Malta, Morocco, Syria, Tunisia and Turkey through a valuation of three key objectives: fiscal proceeds, economic efficiency and the development of the local private sector. The second one focused on the impact of political control on the privatization process in MENA region.

Under **WP4**, the activities of the work team led by FEEM mainly focused on the different meanings of "ownership" and "control", private vs. public. First, methodologies and conceptual framework were described in the "guidelines for data collection on ownership and control structures", submitted in September 2006. Then, the research activity was addressed to the one of the main objectives of the WP4: the analysis of the different patterns of ownership and control as compared with the level of divesting government (central, intermediate, local), with special reference to utilities and public services. The ongoing research aims to identify direct and indirect holdings by central and local governments in large and medium-sized Italian firms. A draft paper has been completed in February 2007 containing the preliminary evidence on the extent of Government owned enterprises (where Government indicates both central and local) and their presence in different areas and sectors of the economy. In the next stage of the research, the weight of these firms in the local economy in term of GDP and employment, and their performance in terms of efficiency and profit, will be analyzed, and different theoretical hypothesis about the determinants of local government ownership of firms will be tested empirically.

Two other questions were faced under this workpackage: on one side, the relationship between the capital structure of regulated firms, regulated prices, and investments, and examine if and how this interaction is affected by ownership structure. On the other side, important results have been achieved with the report studying the evolution of the control structure for a large sample of privatized firms in OECD countries and finds that governments typically transfer ownership rights in State-owned enterprises without relinquishing control rights.

Other important activities are those under **WP5** (Company performance from transition to EU integration). During the first year the work team led by CERGE-EI completed a large original dataset on ownership data of Czech companies publicly traded on the Prague Stock Exchange, delivered in January 2007.). During the second part of the project they started to work with this dataset and completed three research articles (one theoretical and two empirical) accordingly to the work programme. The theoretical paper was delivered in March 2007 as planned and focused on the efficiency and distributional effects of different methods and sequencing of privatizations during the last 15-20 years in the transition economies. The first empirical article investigates the effect of corporate divestitures and subsequent privatization on firms' performance, It show that divestitures increase the firms' indicators of profitability and scale of operations (sales), but do not reduce in a significant way their unit labour cost. The last empirical article investigates controlling potential of the State over privatized firms, studying changes in ownership structure, values of state stakes, and corporate impact on economy employing the large sample of the Czech firms. Both of these two empirical papers were presented during the final conference.

Under **WP6** (Welfare effects on Consumers and employees), the analysis addressed to the study of welfare impact on consumer wealth of privatization, liberalisation and regulation of public utilities under different policy regimes. The first outcome has been the completion of two datasets on welfare measures for consumers and employees delivered in November 2006.

Together with the datasets, the research activity under WP6 produced two papers fitting with the objectives and the deadlines of the project. In the first one, the authors examine the emergence over the last two decades in the EU of a dominant policy paradigm on the reform of network industries with a theoretical discussion of the welfare impact of these reforms. This discussion shows that the dominant policy paradigm oversimplifies a very complex story where the actual success of the reform is conditional to a large number of economic and institutional factors, and that it is far from obvious that is always welfare improving. The second article dresses some questions: are European consumers happy with the services provided by the utilities after two decades of reforms? Is it possible to disentangle the effect on attitudes of privatization from liberalization? This work try to measure the service quality according to the user point of view through an ex-post evaluation method where the customers express their satisfaction after the service is tested. The research activity of this WP has been substantial and all planned deliverables have been completed and submitted as scheduled.

The work team led by Thiess Buettner of IFO, participating under **WP7**, completed the database on fiscal measures and presented the three papers on the effects of privatization policy on welfare. First of all, it put forward a theoretical analysis of privatization incentives for government policy in an inter-temporal context with special emphasis on the role of budgetary institutions. Budgetary restrictions (such as the Stability Pact) are shown to matter significant in explaining the timing and extent of privatization. Then the researchers of this workpackage set up an empirical framework that allows to address the fiscal determinants of privatization in the German context and to compare this with the US case investigated in the third paper, which was presented in February 2007 during the Intermediate Meeting in Prague. All the papers have been delivered with some delay because of some lack of staff but the objectives of the research seem to be met with success.

Under **WP8** (The stock price performance of privatization-related indexes) the first step was the data collection to produce a database with price series of privatization indexes. The sample consists of European firms privatized through public offers of shares in EU15 equity markets between January 1977 and February 2005 (190 stocks). On these stocks CIFRA and FEEM work team carried out a comprehensive analysis of the structure and the evolution of government control rights over the 10 year period 1994-2004 taking into account for indirect voting rights. The data obtained on the evolution of government control rights for the 190 firms have been used for the research on the main objective of WP8: to evaluate the risk and return profile of European listed privatized companies. The focal point of the analysis was to show that theoretically the price behaviour of these stocks may be affected by political risk.

Under **WP9** (Expert interviews and targeted surveys), during the Kick-off Meeting in Barcelona the Consortia members requested Ifo to consider taking over the full responsibility for all survey activities, considering that Ifo has the required know-how, experience and already existing panels throughout Europe (especially in Germany). The survey activities were redesigned and the proposal submitted to the Steering Committee Chairman and to the European Scientific Officer in charge of UPP Project who approved the changes. The broad survey were carried out to obtain information on stakeholders' perception of privatization processes in Europe and to identify interesting partners for in-depth personal interviews on the topic was completed as planned. This part could be an important asset for present and future project, helping to analyse where and how privatization policies are conducted, and to assess the impact of various forms of privatization and liberalisation on competition, growth, employment and gender as well as on various stakeholders and sections of the population in different national contexts. After completion of the interview activities a comprehensive report including all the information received by the two standardized surveys was prepared and submitted within the scheduled deadline.

Furthermore, the research work under **WP10** mainly consisted in preparing the field for the upcoming activities. The work team led by Ettore Scimemi prepared two papers: the first one, after a brief history of the European experience, analyses the public-private ownership debate, then focuses on those articles of the EC Treaty that, directly or indirectly, influence privatization policies. The second paper identifies some policy guidelines which can help divesting governments and policy makers in the organisation of a successful privatization

All the activities presented in this section are discussed in more details, in section 2 and 3 of the activity report.

1.5 End results

Introduction

Privatization is a landmark economic policy of the last two decades both in developed and developing nations. Yet some countries have pursued a consistent and sustained privatization policy as a part of wider reform packages, while in others ambitious programmes have been blocked on their way by adverse interest groups, so that privatization has been sporadic and small-scaled. Furthermore, some governments have typically transferred the majority of capital of State-owned enterprises (SOE) to private investors, while in continental Europe the prevailing corporate governance model in privatized firms appears to be the separation of ownership and control, typified by government wielding power through pyramiding and statutory constraints especially in services of general interest. The gradual shift from State to private ownership of productive assets has been a distinguishing phenomenon in European countries, and a thorough investigation of why and how governments have privatised, and to what extent privatization yielded the desired outcomes in terms of competitiveness, economic growth and social progress is key to design future privatization processes and complementary policies, including liberalization and regulation.

1.5.1. Privatization: political incentives and institutional constraints

Possibly the strongest determinant of privatization processes gas been to raise Government revenue. Even if the demand for privatization emerges from this source is privatization, is it optimal to privatise "simply" to raise cash? The answer is clearly negative, as there are more neutral ways of raising cash, and our research stresses among other things that financial constraints leading to "forced" privatization induce inefficient investment patterns. We also point to the relevance of distributional issues and political economy objectives, as some interest groups may favour privatization even if not needed for other groups.

In this perspective, the Project's **first objective** was to study the political and institutional incentives and constraints affecting privatization, namely:

- a foundation for the link between electoral rules (i.e. majority voting v. proportional systems), political orientation and privatization activity;
- empirical tests of the theoretical results;
- studies of the political economy of privatization and regulatory reform covering the evolution, the sectoral breakdown and the methods of privatization processes also in Euro-Mediterranean Partnership countries.

How privatization can be put at the centre of the debate

A first aspect the research has been to try and understand why the political and social support to privatization can rise and fall following cyclical patterns. These waves can actually be studied on the basis of a model of political competition where the issues are not given exogenously, but rather arise endogenously as parties give them political salience during the electoral campaign. Electoral winning policies may not be intermediate, moderate positions on which the parties would tend to converge. In contrast to the traditional Downsian model, a policy alternative to the status-quo can be initially presented as an innovative, even `extreme' proposal by the challenger party in opposition, seeking to distance itself from the governmental status-quo. Eventually some policy consensus may be created in the voters' concern, often around innovative alternatives, and when the social consensus about the best alternative to the status-quo is sufficient, it makes this policy position to cease to be the subject of controversy.

When in the early 80's, after winning the 1979 election, Mrs. Thatcher introduced her privatization program, this was a very innovative policy fiercely opposed by the trade unions and by the Labour party. However, the majority enjoyed by the Conservative party in Parliament granted her the possibility to implement it, gaining momentum after the 1983 re-election. This success gave political salience to privatization and generated a policy consensus that expanded to other countries. High salience and broad consensus made privatization an attractive issue likely to be adopted by electoral winners. Similar stories could be told for different places and moments regarding once innovative policies, such as civil rights for ethnic minorities, transnational free trade, women's equal rights, a general system of social security, suppression of the compulsory military service, international justice for crimes against humanity, balanced budgets, etc. None of these proposals were initially intermediate compromises between distant alternative policies, but were highly innovative when they were formulated for the first time. However, policy consensus was eventually built on these and other issues after some success. We have presented an agenda-setting formal model of electoral competition. We have used the fundamental analytical elements of the spatial theory, but, in contrast to traditional Downsian models, we have assumed that the policy space is not given, but formed precisely as a consequence of competitive party's strategies. In order to win the election, parties choose to give salience and campaign on those issues on which they expect their policy proposals will obtain voters' broad support. Parties have to trade off the pre-campaign salience of each issue in voters' concerns and the voters' support or consensus in favor of the policy alternatives on the issue. We have found that, although parties will not compete on irrelevant issues (those with both low salience among voters and divisive policy proposals), indeed the issues which are considered the most important ones by a majority of votes may not be given salience during the electoral campaign. The equilibrium results depend only on the probability of victory of the best policy alternatives that parties can propose. This may be a surprising result, but it may be a reasonable one after all. Even if there is extensive public concern on some issue, if there is not a single policy proposal on the issue which can attract broad consensus, focusing on that issue might produce high division and polarization among both parties and voters. Important issues in people's concerns can, thus, be solved through electoral competition only when a policy alternative appears as clearly superior to voters' eyes. In the absence of a likely successful policy alternative, parties can choose not to give salience to the issue, thus maintaining the status-quo policy even if it is unsatisfactory for voters. In the short term, mediocre policies broadly rejected by the electorate, as well as incumbent parties with no good performance in government, may survive for lack of a sufficiently convincing alternative. In the long term, broad policy consensus can be accumulated on an increasing number of issues, but not in the order of importance in voters' concerns. In future work we plan to discuss a multi-election dynamic process. Some of the qualitative findings of the model might be also valid also for alternative settings, including multiparty elections in which two larger parties have strong influence on agenda formation by giving salience to their preferred issues, obtain most votes and lead the subsequent formation of government. In our model, political parties or candidates do not compete to win an election only by `moving' their policy positions across the policy or ideology space, but rather by shaping the space with choices of issues, to which they try to give salience during the electoral campaign. Giving salience to an issue implies proposing an innovative policy proposal on the issue as an alternative to the status-quo policy, and turning it into "news" with some effort (investment) in order to make it relevant for the voters' electoral decisions.

Political orientation, fragmentation and privatization delays

A second relevant aspect is political fragmentation. Both theoretical literature and specific case studies suggest that such fragmentation, which is related to the number of agents with veto power in a given political system, hampers the implementation of policies with significant distributional consequences, such as privatization. A lower political fragmentation favors executive stability and allows incumbent governments to privatize a sizeable fraction of their SOE sector sooner, as the constituency of the "losers" from the policy change is less likely to enjoy bargaining power. On the contrary, highly fragmented political systems tend to disperse decision-making power among different actors, so that executives are weaker and characterized by higher turnover. In this context, the different political actors will hardly reach an agreement about how to distribute the burden of the policy change, and privatization will be delayed by a "war of attrition".

In particular, the studies concentrate on the timing of sales, which varied greatly across countries. We argue that bargaining among political agents may delay the implementation of privatization reforms. Some governments have promptly entered the advanced stage of privatization reforms and raised a significant fraction of their revenues earlier, while others have lagged behind.

In this framework, privatization can be seen as a major adjustment policy with significant distributional consequences. First, privatization curbs political interference, improves managers' incentives, and tends on average to increase the efficiency of firms (Megginson and Netter (2001)). Second, privatization has important distributional effects as it typically involves a transfer of wealth from insiders of State-owned enterprises (such as employees) to outsiders, especially the new shareholders. If a country's political system is highly fragmented, the interest group of "losers" from privatization has voice in the political arena and engages in a war of attrition which delays the efficient policy change. In this perspective, war of attrition models yield therefore the prediction that the expected delay in implementing privatization is increasing in the degree of political fragmentation.

Besides timing, notice that the extent of divestiture also varies greatly across countries. In some countries, governments have pursued a consistent and sustained privatization policy as a part of wider reform packages (i.e., United Kingdom), while in others ambitious programs have been blocked on their way by adverse interest groups (i.e., Belgium), so that privatization has been sporadic and small-scaled.

The Belgian case is certainly interesting in that respect. A significant attempt to restructure and denationalize the public sector was made at the beginning of the 80s but this attempt was thwarted by trade unions in 1983. Only at the beginning of the 90s the process reborned was completed because of the need to meet the Maastricht convergence in 1995. Therefore, one can see that different political institutions matter in explaining a country's ability to implement policies with significant distributional consequences, such as privatization. Particularly, political systems based on majority voting – as opposed to proportional systems – should be more likely to privatize. Majoritarian systems are characterized by a set of institutions which tend to reduce the number of veto players, which results in greater executive stability. On the contrary, consensual or proportional systems tend to disperse decision making power among different actors, so that executives are weaker and characterized by higher turnover.

Another relevant aspect is the political orientation of the government and its re-election concern. According to a largely held view, governments supported by conservative coalitions are more prone to favor market economy, and therefore privatization, than leftist governments, traditionally more inclined to reduce social inequalities and to broaden the size of government. However, center-left governments have also embarked privatization, the Italian case being significant in this respect.

However, the idea that privatization policy is adopted on the grounds of ideological preferences is not completely satisfactory. Theoretically, political preferences should instead matter in the choice of privatization method. Even if governments of all political stripes may privatize, only market-oriented governments design privatization to spread share ownership and foster popular capitalism.

Our results indicate that - in advanced economies - the partisan orientation of the government has a significant impact on the timing, extent and methods of privatization. Governments leaning towards the right of the political spectrum privatize sooner and more. Importantly, they tend to sell shares in the domestic retail market rather than selling them to strategic investors or abroad, as theory suggests. This evidence confirms that privatization is politically motivated, and that a political economy approach is particularly useful in understanding why and how divestiture takes place around the world.

Case studies

These general (theoretical as well as empirical) analyses have been complemented by detailed case studies on the Middle East and North Africa (MENA) region. MENA counties have experimented privatization with varying degrees of success since the late 1980s.

The analysis focuses on the impact of political control on the privatization process. Some scholars contend that privatization can be successful, regardless of the generally participatory nature of the regime, as long as the policy debate on the breadth and scope of the state divestiture process is restricted. Such an approach to the governance of the process allows the authorities to limit the opportunities for potential opponents to create roadblocks. In the early 1990s many international advisers to countries undergoing such a process stressed the importance of insulating policy decision making to remain within a small group of technocrats within the executive. This involved granting special powers in drafting and executing market reforms to the executive, often bypassing legislative and judiciary obstacles and creating what O'Donnell (1999) defined as "delegative democracy." Once the executive muted the institutional obstacles coming from other branches of the government it co-opted the potential losers through the offer of compensation mechanisms to potential losers of the state sector divestiture, mainly to labor (through early retirement, retraining, poverty-relief programs) and business (allowing former managers of state corporations to take over their companies in post-Communist countries or allowing former suppliers to keep out foreign competitors like in some Latin American cases). In so doing, the executive would maintain a free hand and a tight control over the policy process.

A politically controlled privatization can, on the one hand, overcome strong opposition in an environment where the anti-reform interests are stronger than the pro-reform coalition (Haggard and Kaufman, 1992; Belev, 2000). On the other hand, however, this makes privatization highly dependent upon the discretion of the incumbent political leadership whose priorities are subject to change over time, thus affecting the initial policy goals and implementation. As a consequence, privatization may not be fully consistent with other important reform measures, or its progress may not necessarily contribute to a genuine liberalization, especially in the absence of matching steps toward a political opening (Hellman

1998, Schamis 1999).

The comparison of the privatization experience of Egypt and Tunisia through a process tracing method, allows one to analyze in a systematic fashion various factors which often cannot be measured statistically. The selection of Egypt and Tunisia rests on the fact that these are countries experiencing divestiture of state-owned assets and functions under strong governments which, in theory, provide the best context for the exercise of political control. Moreover, to enrich the analysis we also make some comparisons with other MENA countries, as well as with the references to the experience of CEE and Latin America. Within this framework our study shows the limitations of tightly controlled privatization when compared to the market reform package as a whole. The effectiveness of a piecemeal policy, which does not pay sufficient attention to the market context where privatization takes place proves extremely limited.

Privatization and the financing of local public authorities

Another factor which the literature acknowledges as central to privatization decisions is the tightness of the budget constraint. While most existing analyses look at central governments, which have been affected by such constraints especially during the process leading to the common European currency, the study carried out has looked at local authorities.

Local bodies are assumed to have some power over taxation and must decide upon some public investments in an intertemporal setting under conditions of revenue shocks. Exactly how local governments manage to determine their long- and short-run policy objectives while complying with basic accounting cash flow constraints in a dynamic and uncertain environment - subject at all times to conflicting political imperatives - is not well understood. The institutional structure within which local bodies operate typically include annual budgeting for expenditures, compliance with accounting standards for the disclosure of expenditures, revenues, and asset and liability acquisitions and dispositions, adjustments of tax and other revenue-generating policies through the actions of legislatures or other governance bodies, and constraints imposed by financial and other markets, all plausibly play some role in determining the evolution of fiscal policies.

In particular, without borrowing restrictions, the optimal policy is characterized by smooth time paths of taxes and public investment. While the introduction of formal borrowing restrictions leads to some precautionary savings, it gives rise to fluctuations in public investment, and hence in privatization plans, in response to adverse (or favourable) revenue shocks. To analyze these issues, a theoretical and empirical analysis of the dynamic evolution of government finances in an explicitly inter-temporal setting is developed, within which governments may accumulate or decumulate real and financial assets while facing fundamental economic uncertainties that produce revenue fluctuations

This theoretical framework provides the foundation for an empirical analysis of a 25-year panel of more than 1000 municipal governments in the US. The results highlight the importance of access to capital markets not only for purposes of long-run optimization of taxation and infrastructure-related public service provision but for purposes of adjustment to short-run stochastic shocks. Even when fiscal policies are optimized over long planning horizons, governments must still adjust to short-run shocks, and, in doing so, they face trade-offs between the pursuit of long-term goals and compliance with short-run constraints. Restrictions on access to capital markets change the financial environment within which long-term decisions are made and implemented as well as the capacity of governments to adapt to temporary stochastic fluctuations.

Aside from own revenues raised from local taxes and charges, local governments in European countries rely on intergovernmental revenue obtained from higher levels of government. The literature on fiscal federalism has justified this kind of intervention as a means to induce the local governments to provide specific types of public goods, to redistribute among lower level governments, and to ensure efficiency under conditions of intergovernmental externalities. The more recent literature emphasizes, however, that intergovernmental transfers give rise to important questions of governance, since higher level governments allocate funds on the basis of conditions which are subject to strategic choices of local governments.

One important institutional dimension in this regard is the role of fiscal equalization transfers. While most countries assist sub national governments by means of vertical grants, some federal countries, such as Australia, Canada, Germany, or Switzerland, entertain redistributive transfer schemes that explicitly aim at equalizing revenue capacities across subnational governments. These transfers might be quite effective in providing fiscal assistance in case of adverse revenue shocks because they are formally related to the taxing capacity of a jurisdiction and are not subject to the immediate discretion of policy makers. However, little is known about the comparative performance of these fiscal equalization systems and more standard systems of vertical grants in maintaining fiscal balance and about associated governance problems.

The results confirm that a substantial part of fiscal adjustment is due to changes in intergovernmental transfers: in present value terms about 34 cents of a permanent one euro decrease in own revenues are compensated by subsequent changes in fiscal equalization transfers. Therefore, the contribution of intergovernmental transfers in maintaining fiscal balance is found to be two to three times higher than in the case of US municipalities. Nevertheless, budget components such as own revenues display larger fluctuations in the German case. This supports concerns that the insurance against local revenue shocks provided by the fiscal equalization system is creating a moral-hazard problem.

While municipalities in Germany also enjoy some autonomy in expenditures as well as in taxation they are subject to a comprehensive system of fiscal equalization transfers. Given these differences, the German case offers interesting opportunities for comparisons with the case of US municipalities. The empirical results support the idea that fiscal equalization for budget balance plays a major role in shaping privatization policies at local level. The degree of fiscal assistance provided by intergovernmental revenue is much more significant than in the case of US municipalities. At the same time, however, rather strong fluctuations can be seen in own revenues, which may be related to the strong reliance of municipalities on the business tax (a local profit tax). This suggests that the large amount of insurance provided by the system of fiscal equalization might induce the municipalities to rely more on the volatile business tax rather than using property taxes as the US counterparts.

1.5.2. Private and Public Control of Firms

The Project's **second objective** was to analyse the interactions between private and public ownership and control of firms, especially referring to regulated markets and SGI. More particularly:

- a framework to evaluate the trade-offs between private and public ownership and control of corporations, and identify (if any) the optimal government's stake in models encompassing issues of regulatory governance;
- empirical analyses on the evolution of ownership and control structures of privatised firms assessing the long term effect of changes of ownership structure on firm value in OECD economies and in the Czech Republic;
- empirical analyses on the different patterns of ownership and control as compared with the level of divesting government (central, intermediate, local), with special reference to utilities and public services, and taking into account also legal and statutory constraints embodied in the so called "golden share provisions".

How State control survives privatization

Governments all over the world have either sold or are selling large blocks of their ownership positions in corporations to the private sector. In terms of flows, privatization transactions, including share issue privatization (SIP) and private placements, have raised globally revenues of US$1,230 billion during the 1977-2003 period, about one fifth of total issuance on public equity markets. Yet, stories in the popular press suggest that the roll back of the State has been incomplete: privatisation and persistent State control apparently coexist.

Governments have often separated ownership and control in privatized companies by means of pyramids, statutory restrictions and special-class shares that grant them exceptional powers. According to recent estimates, European governments own shareholdings in (listed) privatised companies worth approximately €250bn. If we add to this figure other financial holdings and the value of non corporatised assets, a conservative estimate of State property in the EU approaches €1trn.

Italian privatizations provide a revealing example of this reluctance to relinquish control in State-owned enterprises (SOEs). We show that many privatizations of a SOE are characterized by the sale of equity without a corresponding transfer of control rights. This may happen because the government remains the largest ultimate shareholder of the company, although it no longer owns 100% of the stocks, or because it enjoys veto or special powers through its possession of so-called "golden shares." We document this evolution of corporate control by carrying out a comprehensive analysis of the structure of ultimate control (voting) rights in a sample of 141 privatized (publicly traded) companies from developed economies, over the period 1996 to 2000. We find that the most common privatization outcome is that the State remains the largest ultimate owner. This is true for about one third of so-called "privatized" firms.

Consistent with earlier findings by Jones, Megginson, Netter and Nash (1999), a widespread use of control restrictions and golden shares can be documented. These mechanisms are particularly common amongst privatized companies in which the government is not the largest shareholder. This combination of evidence allows us to conclude that through ownership or golden shares, governments are able to maintain control of almost two thirds of privatized firms. The instruments used by governments to retain control over privatized firms differ, to some extent, across countries. For example, while governments are unlikely to keep large ownership stakes in privatized firms in common law countries, golden shares are widespread in these same jurisdictions. Thus, there seem to be some substitution in the channels used by governments to maintain their influence over SOEs.

State Control after privatisation in the Czech Republic

At the beginning of the transformation process in Central Europe, privatization was largely considered the foundation of the entire transition process. The transfer of ownership rights was seen by most academics and policy makers as crucial for the efficient allocation of resources and economic growth (Estrin, Hanousek, Kočenda and Svejnar, 2007). Truly, transition economies carried out a major ownership transformation that made the share of the private sector in GDP increase from extremely low levels to between 60% and 90% (see EBRD, 2001 and 2006). They also strived to establish market-oriented institutions and a legal system that would improve the role of the state in providing infrastructure vital to the newly emerging market economy (state governance).

Privatization schemes in many European emerging economies involved the creation of a special government agency that assumed the role of the administrator of state property. The state often remained the ultimate owner of numerous firms long after privatization was concluded, a situation that has been documented for the Czech Republic. In the Czech Republic, the National Property Fund (NPF) acted as the governmental administrator of the property that remained in the possession of the state. As the NPF was dissolved at the end of 2005, it is relevant to study the extent of state control potential in privatized firms from a long-term perspective. In this paper, we examine the dynamics of changes in the structure of ownership, the extent of state ownership and the potential for state control in privatized Czech firms over the period 1994–2005, i.e. from the end of privatization to the dissolution of the NPF.

The identification of the extent of state control is important as state control in privatized firms may have potentially negative effects due to several reasons. Shleifer and Vishny (1994) argue that inferior performance (in terms of value maximization) of state firms can be expected because state officials are prone to impose on the management of state companies a variety of goals, such as the minimization of layoffs, political patronage, or protecting other state firms' markets, and these goals differ from those associated with the quest for economic efficiency. Hence, the performance of state-owned enterprises (SOEs) suffers from the above political costs as well as agency costs (Shleifer and Vishny, 1994; Qian, 1996). Further, following other-than-economic objectives, firms with state control are less likely to innovate and restructure their line of production. Restructuring was often delayed in privatized firms where the state retained various degrees of ownership.

Further, direct or indirect state control can provide grounds for retaining or creating a monopoly, which is generally known to produce lower output at higher prices when compared to standard competition. On other hand, monopoly power also poses a dilemma for the state as owner because a firm that is privatized with monopoly power can be sold for a higher price than if it is divided into units to create a more competitive market structure (Estrin, 1994).

We quantify the extent of potential state control over the assets of privatized firms in the decade after the end of the privatization period. Complete data about assets, shares and means of indirect control in privatized firms enable us to formulate a relatively decisive conclusion about one phenomenon of the Czech transition which to date, due to the non-existence of relevant data, could not have been studied at the appropriate level. Based on the data analysis, we suggest taking into account the potential of the state to control the assets of privatized firms, since firms in the economy under such potential control cannot be considered truly private. This study supports the conclusion that "the role of the state is far more important than it may appear" at first glance and that "the state is still an indirect shareholder" in "an important sector of the economy".

Focus on "municipal capitalism"

We have already stressed that the conventional economic approach hinges upon a dichotomy private/privatized company, without taking into account the real complexity of mixed ownership, where control rights are exerted via structures such as pyramids, statutory constraints, and special powers of public shareholders. This has been largely used at local level, where regional and local authorities are very often present within firms which are said to have been privatised. Public presence is in firms in general is widespread – in mixed forms as well as in pure ones – in the Italian case, which has been analysed in detail.

A recent debate in Italy has stressed the relevance of the so called "municipal capitalism", i.e. of the increasing presence of firms created and owned by local governments in various sectors. The research first identifies direct and indirect holdings by central and local governments in large and medium-sized Italian firms. A second task is to provide evidence on their impact on economic activity, and on their operating and financial performance.

We can show that more than 400 medium-large firms are participated by local governments in Italy, employing more than 200.000 people, and producing on average more than 1% of total national GDP. In some region this figure rises to more than 6%. The public presence is not limited to traditional "public services" (or services of general interest) but is very common in sectors, which are normally open to competition.

Mixed firms are then compared to totally public firms, showing that in mixed firms not only profitability is higher, but all efficiency indices show better performances.

1.5.3. The Effects of Privatization Policies

The Project's **third objective** was thus to evaluate the effects of privatisation policies on several stakeholders, such as:

- consumers, analyzing empirically the impact of privatisation, liberalisation and regulation of public utilities on individual and household welfare under different policy regimes, with special reference to SGI such as water supply, gas, electricity and telecommunications;
- taxpayers, studying the role of privatisation in stabilizing the current budget and in maintaining fiscal balance in the long-run both at the local and central level;
- shareholders, evaluating the stock market performance of European listed privatised firms in order identify the risk and return characteristic of this particular investment;
- employees, analyzing the long term effect of privatization on employment levels and wages in selected European countries.

The effects of privatization in Transition Economies

This paper is motivated by the ongoing debate among economists and policy makers about the efficiency and other economic effects of privatization of state-owned enterprises (SOEs). Our goal is to evaluate what we have learned to date about the effects of privatization from the experiences during the last 15-20 years in the post-communist (transition) economies and, where relevant, China.

Our analysis highlights several significant shifts of emphasis in the literature in recent years. Firstly as ownership structures have evolved, research interest has shifted from comparing categories of domestic owners (e.g., insider versus outsider) to contrasting domestic and foreign ownership, to a thorough study of the performance of privatized (as compared to de novo enterprises) and of the impact of concentrated v. dispersed ownership. Researchers have also increasingly noted that policies and institutional development have diverged between the CEE and CIS countries, with the former increasingly adopting European Union (EU) rules and joining the EU, and the latter proceeding slower in introducing a market friendly legal and institutional system.

Starting from the macroeconomic studies, we find that the results suggest that privatization, especially when accompanied by complementary reforms, may have a positive effect on the level of aggregate output or economic growth.

As to the impact of privatization on total factor productivity (TFP), we find that in CEE the overall effect is mostly positive during both the early and later transition periods, but that the effect of privatization to domestic owners is quantitatively much smaller than that to foreign owners, and that it is greater in the later than earlier transition period. In CIS, privatization to foreign owners yields a positive or insignificant effect while privatization to domestic owners generates a negative or insignificant effect. Concentration of ownership is important, with majority private ownership having mostly positive effects on the level of TFP. The overall positive effect is again driven primarily by foreign owned firms. The effect of majority domestic private ownership tends to be positive but smaller in magnitude. Studies that distinguish between privatized SOEs and newly created private firms suggest that de novo firms are more productive than or at least as productive as SOEs privatized to domestic owners.

The effect of ownership on profitability has been estimated mostly in CEE and shows a positive but very small and often non-significant effect of privatization to domestic or foreign owners on profitability levels in the early as well late transformation periods. In the same way, the effect of privatization to domestic and foreign owners on the rate of growth of profitability is (at most) very small. The effect varies across types of ownership, and concentrated domestic private ownership, managerial ownership, and to a lesser extent foreign ownership tend to have a positive effect on profitability, while state keeping a golden share or concentration of worker ownership appear to be unrelated to profitability.

The effect of privatization on firm revenues, capturing the effect of privatization on the scale of operation of the firm, is mostly strong and positive. In terms of revenue growth, we observe in CEE a high positive effect of privatization to foreign owners in the early period and a small effect in the later period, as well as an insignificant effect of privatization to domestic owners. Overall, the studies of CEE and CIS countries indicate that privatization tends to have a positive effect on the scale of operation, while studies of the effect of private ownership on the rate of change of scale of operations (from CEE, CIS and China) suggest that this effect is not statistically significant except in some well defined categories of ownership.

Estimates of the effect of privatization on labor productivity (not controlling for the use of others inputs) are similar to the TFP results -- the effect of privatization is primarily positive or insignificant.

In terms of the effect of privatization on employment, the estimates indicate that there is a tendency for privatized firms, especially those with foreign owners, to increase or not to reduce employment relative to firms with state ownership.

Studies of the effects of ownership on wages find that state ownership is associated with lower wages in some countries, such as Russia and former Czechoslovakia, but not in others, such as Poland.

Studies that have analyzed the effect of privatization on other dependent variables show that (a) privatization results in higher exports and greater efficiency, as measured by the cost of inputs relative to sales, Tobin's Q, and soft budget constraints, and (b) privatization to foreign firms leads to more restructuring and sale of assets, greater likelihood of payment of dividends, and smaller likelihood of default on debt. These results exhibit a pattern that is in line with the above measures of performance.

The effect of privatization in emerging markets – a look at micro data

Corporate divestures (including asset sales, spinoffs, breakups, and carve-outs) play an important part in advanced market economies and they have been widely researched in the literature. The Czech Republic constitutes a particularly useful laboratory for analyzing the effects of divestitures and privatization on financial and economic performance in emerging markets. During the late 1980s and early-to-mid 1990s the country had many features found in other emerging market economies, but the variation in the values of the relevant variables was much greater. In the Czech Republic these processes were much more pronounced than in most other economies.

The structural and institutional features observed in the emerging market economies in general, and the Czech Republic in particular, have allowed us to test two competing hypotheses with respect to divestitures and privatization:

1. Divestitures and privatization have a positive effect on the performance of the resulting units by eliminating inefficiencies such as diseconomies of scale of large SOEs, weak managerial incentives and information asymmetries that existed prior to economic liberalization and reduction of state control;

2. Divestitures and privatization have a negative effect on the performance of the resulting units because of weak corporate governance, waning government coordination and regulation, unclear property rights, and underdeveloped legal and institutional framework that exist in emerging market economies.

With respect to privatization, we have also tested whether the nature of the effect depends on the type of the new ownership structure.

Divestitures and privatization have a number of significant effects on corporate performance. The average divestiture increases the firm's profitability and scale of operations (sales), while the effect of privatization depends on the resulting ownership structure. The overall evidence for divestitures is consistent with the hypothesis that divestitures have a positive effect on performance. Reducing state ownership is positive for some performance indicators but insignificant or even negative for others. Industrial firms as owners improve or do not hamper performance and in that sense they behave consistently with our first hypothesis. Financial companies and individuals as owners are mostly associated with no improvement and in some cases significant declines in performance, thus providing evidence that is consistent with the second hypothesis.

The effects of privatisation policy on political risk and asset prices□

The government plays a fundamental role in most countries. The size and scope of government varies around the world and over time, and in many economies it accounts for a sizable fraction of GDP. Yet the broad discretionary powers enjoyed by the State can also hurt economic agents when incumbent governments raise taxes, revise legislation to cater specific constituencies, renege contracts, or exert their powers to interfere in the operating activity of firms.

The effects of the economic activity of the state are not only important and widespread, but also quite unpredictable overtime. The investors must form expectations about the risk that a future political event will change the prospects of profitability of a given investment. This is what economists and political scientists usually define political risk.

Political risk has been predominantly analyzed in emerging markets.

Our study shows that political risk is also potentially relevant in developed economies with mature financial markets. The recent case triggered by the bid for Suez, the large French multi-utility, by Enel, the Italian electricity giant, provides an interesting example of the relevance of political risk in European stock markets. At the end of February 2006, rumours spread that Enel was ready to make an hostile bid for the Suez Group. This news prompted an immediate reaction by the French government who announced a merger plan between Suez and Gaz de France (GdF), the government controlled gas utility (now the merger has been completed). This example suggests that political risk matters also in developed economies as the profitability of companies traded in the stock market may be affected by sudden government actions.

In our view, the issue is not if there is a risk premium component associated with political risk but how we can measure it and how large it is. We claim that it is possible to find a suitable proxy for political risk by looking at companies which have been privatized to some degree. Our central hypothesis is that privatized companies – such as Suez – are particularly sensitive to systematic political risk factors. Indeed, there are historical reasons why certain firms used to be under public control and governments may try to regain political influence in these companies after privatization. First, SOEs are typically large firms with a broad clientele, they often provide services of general interest and manage strategic infrastructures with high sunk costs. As such, they are severely exposed to political interference in the form of expropriation of quasi-rents. Second, privatized firms can also be used as tools in domestic or foreign policy in order to raise fiscal revenues, to absorb unemployment, to please consumers with affordable tariffs and universal service, and to preserve national security in strategic supplies. Finally, the pricing of the shares of privatized companies can also be designed to achieve key political objectives, notably re-election (Biais and Perotti, 2002). A typical channel through which governments may affect the operating activity of the firms is regulation which can be easily captured especially when regulators are not fully independent from the executive.

In our analysis, we have tested the effect of residual state ownership and control on the expected returns of privatized companies. We track the evolution of government control rights in firms privatized in EU15, and study the long run performance of several portfolios built on different quartiles of government control rights for the 1995-2005 period. Using the time series multifactor regression approach of Fama-French, we find that the portfolio based on the bottom quartile of government control rights - comprising fully privatized companies - significantly outperform portfolios formed by stocks with higher government's residual stakes. The difference in annualized average returns ranges from 5.9 to 3.8 percent.

If a political risk premium can be identified on the basis of residual state ownership in firms, the issue becomes to test whether this factor can capture sensitivity to a common and thus undiversifiable risk affecting asset prices. In other words, we are interested in testing whether a "political risk beta" explains the expected returns of a fully integrated area such as EU15.

We conclude that a low level of residual state ownership may proxy for sensitivity to common and thus undiversifiable political risk factors, and that the notion of political risk beta is useful for a better understanding of returns of European equity markets.

The perception of reforms of Services of General Interest: the viewpoint of consumers and experts

In sectors supplying services of general interest privatisation has been widespread in Europe and other countries, and it goes hand in hand with regulatory reforms and liberalisation. However, in some cases the perception of consumers is that the outcome of this exceptional amount of reform effort is not totally satisfactory. The research question addressed in a part of the analysis is thus whether European consumers are happy with the services provided by the utilities after two decades of reforms.

While the empirical literature has usually focussed on changes in efficiency of the industry, rather surprisingly the research on the impact of utility reforms on consumers is less developed.

Our study has explored perceptions by consumers, i.e. subjective data on happiness with three dimensions of services of general interest (SGI): accessibility, price and quality. Thus we have not directly studied whether utility reforms explain variations in welfare of consumers across countries and time periods, but whether they are correlated to their perceptions. There are two reasons to consider data on social attitudes. First, because they are important per se. Policy-makers and regulators are well aware that SGI reforms are in the forefront of public debate in the European Union (the widespread concern about the Bolkenstein Directive on the liberalization of services being a clear example).

Second, subjective data can be a complement to objective evidence in order to evaluate the welfare impact of reforms. Ideally, for example, one would use both detailed microdata on price paid and expenditure by households, or on objectively measured quality, along with individual attitudes on these dimension of SGI, to test economic welfare change and compare them with 'happiness' measures. If the two measures do not correlate, this fact would need further research to understand whether the cognitive process by the consumer is biased, or whether the objective statistical evidence does not capture details in SGI provision best known to the user (e.g. aspects of quality, or of price discrimination not reflected in average price indexes).

Although an unconditional analysis across countries points out that some countries, notably Italy, Greece and Portugal show a significant extent of dissatisfaction, once one controls for individual and country fixed-effects the picture is significantly more complex. While some individual characteristics in the samples, and some macroeconomic controls may contribute to explain the degree of satisfaction, the impact of regulatory variables is also notable. Notice however that disentangling the perception of privatization from those of liberalization proves extremely complex. Among the main conclusions, we can list the following.

a) For telephone price and for electricity access, price and quality, consumers' satisfaction is higher in countries where public ownership is large, but the reverse is true for gas.

b) One obvious measure of liberalization is the market share of the incumbent, and one would expect that the smaller such a share, the more competitive is the market, the lower the price for a given quality, and the higher the access, hence the higher consumers' satisfaction. This expectation is rejected by data for gas quality, where satisfaction is positively correlated with the market share of the incumbent, and in the other cases it is not significant.

c) A second liberalization variable is 'free entry': this works as expected for telephone access and gas price, but not for telephone price, gas access and quality, and electricity quality.

d) Vertical integration has a negative impact if any for gas services satisfaction, but a positive one for electricity services.

Notice that as privatisation was probably mainly driven by concerns for Government revenues, it may be hardly surprising that consumers are not totally happy with the result. However, it is hard to tell whether this dissatisfaction has to do with a well founded perception of the current situation, or rather by the fact that citizens in many countries feel less protected by the combination of privatisation and regulation than by direct public ownership.

In all cases, notice that any analysis of the consequences of privatisation (and reforms) would require a counterfactual exercise which is hard to construct in general cross country analyses.

However, it is interesting to see that analogously "non enthusiastic" opinions have been recorded in the interviews among numerous business and opinion leaders across Europe. The survey was sent out to 300 country specialists (managers and professional analysts) throughout Europe.

The survey revealed that according to the surveyed experts prices throughout Europe have, except for telecommunication services, not declined significantly due to privatization. A majority of the experts believed that energy prices have even risen after the privatization of the former incumbents. When asked about the development of prices in the water and gas sector most of the experts either stated that prices have not changed significantly or claimed that prices like in the energy sector have risen too after privatization. When asked about the development of wages after the privatization process around half of the experts stated that privatization has not brought about a significant change. However, overall more experts claimed that wages have risen after privatization than fallen. This does not hold for Germany in which case more experts claimed that privatization has resulted in a fall of wages in every sector of the utilities.

When questioned about the effects of utility privatization on employment, the experts drew a relative negative picture. On balance in all EU member countries privatization led to a decline of employment. Overall the experts drew a positive picture regarding the effects of privatization on the quality of services and consumer choices. On account of growing competition, the quality and consumer choice increased particularly in the telephone and electricity sector. However, except for the telecommunication sector more than 50 percent of the experts stated that quality has not improved in the gas, water and electricity sector.

1.5.4. Policy Implications: making privatization deliver

Drawing some comprehensive policy recommendations on the issue of privatisation is an important final aspect to consider. The strategic policy questions we want to answer are:

- what principles should guide the overall approach to privatisation;
- what political and institutional factors favour the implementation and sustainable large-scale reform programme, with special reference to SGI;
- what is the appropriate role of national and sub-national governments in shaping the divestiture process, how to deal with the potential conflict emerging at a different level of jurisdiction;
- to what extent privatisation may contribute to the creation of a Single Market and especially to the integration of European securities markets;
- how an appropriate management of privatisation can improve the credibility of regulatory policies aimed at improving the competitiveness of the European economy;
- how the complementary liberalisation and regulatory policies should be designed to make privatisation deliver the most desirable outcomes
- how the liberalisation of SGI-markets could lead to new models of public-private-partnership;
- how should privatisation be designed to minimise the adverse social effects and the impact in terms on distribution of wealth.

The aim of this paragraph is to present an overview of the most important phases of the privatisation process. It will deal with the legislative and institutional level of responsibility for privatisation, with the choice of the privatisation candidates, with the restructuring decisions, with the valuation of the SOEs and finally with the choice of the privatisation methods. All these aspects are important parts of the entire privatisation program and must be taken into consideration to develop a whole and complete selling procedure.

The institutional set-up

Before deciding which assets to sell or sectors to include in the privatisation program, a government must set the legal framework for privatisation. Building such framework in an appropriate way is a crucial aspect of the process.

First of all, finding the right balance in the relationship between the parliament and the institutional actors has been a key issue in privatisations. In the same way, setting an appropriate balance between politics and administration is equally important. Without denying the political relevance of other parts of the implementation of the programme, however, continuous political interference should be avoided with a proper delegation of powers.

In this perspective, the privatisation process may give birth to new institutions needed to manage different phases of the transactions. Specific institutions may be set up to act as executing agencies for large national privatisation programs: restructuring agencies, valuation agencies; institutions that control the transparency and correctness of the procedures of sale with the intent to minimise the fraud or corruption; agencies that control the fulfilment of the eventual obligations imposed to the buyers in the sale agreement and privatisation funds that can enable to avoid the atomisation of shareholding, give small shareholders greater voice in corporate bodies, improve corporate governance, and develop financial intermediaries and markets.

Whatever the chosen institutional structure, certain conditions have always to be met for a successful privatisation program.

SGIs and the role for the State

After the implementation of the legislative and institutional framework for privatisation, the very first step a privatising government must take is to decide which state-owned enterprises and sectors should be slated for privatisation. This choice can be extremely difficult and contentious , especially when the political context is very fragmented.

The first group usually encompasses small industries operating in competitive industries that eventually require only a small capital investment while the second group, instead, traditionally includes large industries operating in monopoly markets that require greater preparation prior to sale.

In managing SOEs governments often try to pursue potentially conflicting objectives of social and commercial nature. In order to solve this problem, a change in the role of the State may be appropriate: the state and its regulatory institutions could take care of the public interest and of the quality of the service (the social objective), while the firm owners could be private, profit-oriented shareholders pursuing profit maximisation and assuming the commercial risks associated with the economic activity (the commercial objective).

Establishing that something can be privatised does not mean that it should be privatised. In each instance, the costs and benefits of public versus private provision of a given service, including the associated transaction costs, as well as economic, financial, political, and social consequences of the planned privatisation should be analysed.

Privatisation is probably the obvious solution only when the commercial/profit related objectives are predominant and can be separated from the public interest objectives in a meaningful way. When the commercial objectives are limited compared to the public interest, the case for privatisation is less clear cut.

The sequencing decision

Another important policy decision that a privatising government should take is the order by which assets are privatised. This aspect can be particularly important for the privatising government in order to build reputational capital with investors and domestic support for the privatisation program. Successful privatisations, in fact, can help government to build credibility for the program, both with potential investors and with the public. In order to meet this objective, in the European countries the sequencing decision has often been based on the quality of the assets (with companies with good performance being privatised before companies with poor performance), and on the complexity of the assets in terms of their market structure and the need for a regulatory framework (with assets in competitive markets being disposed off before assets in non-competitive markets).

An important and difficult decision that most governments confront early in any privatisation process is whether an SOE should be restructured before divestment in order to create a viable commercial enterprises. The general objective of the restructuring phase is to render the candidate company desirable for potential investors.

To render this phase effective, however, governments first of all need to carry out a general mind-changing in managing the companies chosen. During the restructuring phase governments should commit to hard budget constraints, to establish performance contracts which tie managers' remuneration to the performances of the company, to enhance the manager's independence, and to abolish all preferential treatments of SOEs. The playing field should be levelled for these enterprises and those in the private sector. If this does not happen, all the (financial and operative) restructuring efforts described above may be jeopardised by the soft-budget constraints that would continue to be imposed on the company to be privatised.

1.5.5. The Privatization Methods

Several methods of privatisation have been used, and the choice depends on a long list of variables which can include: the specific characteristics of the SOE; the history of the country; the domestic legal, economic and financial environment of the country and the objectives of the privatisation program.
It is possible to single out three main privatisation methods:

1. restitution, which was particularly used in the Eastern countries;

2. voucher privatisation, which involves the distribution of vouchers free of charge or at a nominal price to eligible citizens, who can then use them to buy a stake in privatised companies;

3. sale of state property in the form of:

- private sales – sometimes in the form of management and employee buy-outs
- public offerings

Restitution is appropriate when land or other easily identifiable property that was expropriated in the past can be returned either to the original owner or to his or her heirs without too many delays or legal complaints.

Voucher privatisation

The choice of vouchers was due to a combination of (i) the aim to privatise large enterprises quickly but (ii) the desire not to sell them exclusively either to foreign investors or to the incumbent management, and (iii) the lack of functioning capital markets. The programs implied the transfer of the ownership of public assets to eligible citizens through the public distribution of vouchers free of charge or at a nominal price.

This helped to build a reasonable political consensus, and made privatisation politically irreversible since it allowed a certain percentage of the population in each country to become effectively capitalists.

Compared to the expected objectives, the record on voucher privatisation has indeed been quite poor. The cash inflow was almost nil, while especially privatised companies needed new capital for their sustainability. Small investors have immediately sold their shareholdings to people that had the available funds in order to realise a quick capital gain. Most of the time, the buyers were the previous managers of the privatised company who, in this way, became the new company owners. Finally, the governments often retained effective control of the banking sector and these banks continued to suffer political influence, so that even privatised firms continued to face soft budget constraints for indefinite periods.

In the future, it is doubtful that new countries will decide to start voucher privatisation programs. Nowadays, most countries have financial markets that give them other alternatives.

Sale of state property

The sale of state property can take two forms. The first is a partial or total private sale of state owned enterprises to an individual, an existing corporation or a group of investors. The second form is a share issue privatisation (SIP), in which the government sells some or all of its holdings in an SOE to investors through a public share offering. This latter form is similar to an IPO in the private sector, but whilst private IPOs are structured primarily to raise revenue for the company, SIPs are usually structured to raise money for the divesting government and to achieve political objectives.

The choice of whether or not to use public capital markets is based not only on the revenues

that the seller (in this case, the government) can receive through one or the other methods but also on other factors, such as the development of the capital market, the political and legal environment of the country, and the specific characteristics of the firm.
As for the first category, some considerations may suggest that when the domestic capital market is not well developed, private sale is a more appropriate method of sale than SIP. On the other hand, however, governments may be willing to sacrifice some of the proceeds in an effort to spur the growth of rising financial markets. In fact, a carefully structured and well-articulated program for privatising major state-owned entities, combined with efforts to establish a suitable regulatory and legislative framework, can give a stock market the needed boost in size and quality.
As for the political and legal environment, the Government's stability is the first fundamental variable. On the one hand, it may affect the investors' perception of a nation's commitment to policy. The orientation of the governments may also be relevant. Right-wing governments, in fact, are generally deemed to be less intrusive (i.e. their commitment to protect private property rights in general is considered higher) than left-wing governments. Thus, there could be a positive relation between right-wing governments and investors' willing to buy.
The protection of investors' rights, instead, can be considered an important variable that influence not only the investors' willing to buy but also the government's choice between selling a SOE in the public capital market or in the private capital market. According to La Porta et al., in fact, countries with stronger protection for minority shareholders have a higher company valuation and a lower concentration of ownership.
Finally, firm-specific characteristics play an important role in the choice of the privatisation method too. The expected post divestment performance of the SOE may also influence the government's choice of the privatisation technique since the public perception of the newly privatised firm's performance is important to the success or failure of the privatisation program. In this perspective, share issue privatisations involve the greatest amount of reputational risk for the state, because the sales are frequently preceded by extensive promotional campaigns and often create thousands of small, first-time shareholders.
The industry where the SOE operates may be a relevant factor in deciding whether a government privatises through an SIP or a private sale. Industries such as defence, transportation, and energy could be of such strategic significance that foreign ownership may be unacceptable. A SOEs' size is another important variable. The larger the SOE, the more likely it is to be sold through an SIP, which entails considerable fixed costs.
An ideal method for valuating and pricing the company to be privatised does not exist, but some important principles can be kept in mind during these phases. The methods of valuation and pricing should be transparent, rigorous yet flexible, adaptable, realistic and in conformity with generally accepted principles.

If a government decides that a private sale is the optimal method of privatisation, it faces a series of strategic decisions that depend on the objectives it desires to achieve. In particular, governments face some key decisions.

1) First, it must decide whether to conduct all aspects of the sale itself, or to delegate some of the key tasks to an investment bank. Hiring reputable third parties to value and to conduct the sale increase the credibility. On balance, most governments usually have used third parties only for large and profitable private sales.

2) The second strategic decision a government using private sales must face is whether and how to structure the selling terms in order to maximise the sales price and achieve other political and economic objectives.

3) The final strategic decision a divesting government must take is whether to conduct private sales through competitive biddings (auctions) or direct negotiations with pre-selected potential buyers. If the revenue-maximizing answer is probably obvious (auctions), governments often prefer to conduct direct negotiations in which they can more easily achieve different objectives.

Private sales have advantages and disadvantages. They are typically carried out with minimal legal restructuring, require less planning and can be executed much more rapidly than SIPs. They also have the advantage of being feasible in the absence of a well-developed and sophisticated market environment and can be used to attract foreign direct investment into a country. When absolutely necessary, they can also ensure that truly strategic assets remain in domestic hands and allow governments to craft sophisticated sale terms to meet political, social, and corporate governance objectives. Though private sales offer key advantages, they also have several disadvantages relative to SIPs. First, private sales typically yield significantly lower sale proceeds than do comparable share issue privatisations and may not always result in the highest quality buyer. Second, private sales do nothing to promote development of the national stock market. Third, in terms of process integrity their main drawback is that they do not provide the same degree of transparency as public offerings and therefore they may potentially be prone to corruption. Finally private sales to strategic investors are especially vulnerable to competitive failings. The state is often tempted (or entrapped) into selling its controlling shares to local interests, with negative results for competitiveness.

Privatisation through public share offerings is an open competitive process which uses the stock market. This is typically considered the most transparent privatisation method; it enhances the development of capital markets, create broad ownership, and, if successful, may help the government to build a reputation for future sales. Moreover, it is a good mechanism to attract foreign investment, both from institutional and non-institutional investors.

The main disadvantage of this method is its cost, both because of transaction costs (technical and legal assistance) and in terms of the under-pricing which is often necessary to compensate for the asymmetric information between the seller and the (potentially large number of) buyers.

Governments usually have used share issue privatisations to pursue economic and political goals like the reduction of national budget deficit (preferring secondary share offerings), the promotion of popular capitalism (setting high level of under-pricing and allocating shares as widely as possible to citizens) and the growth of government popularity (setting high level of under-pricing in order to guarantee high capital gains for investors).

Governments involved in privatising an enterprise through an initial public offering must face a number of decisions, like the reorganisation of the SOE, the choice of the advisors, whether to retain a golden share, how to allocate the shares to different classes of investors such as retail, institutional, foreign and residents and the setting of the share price.

In particular, when a company is too large to be sold at one time, the government can benefit from selling it gradually through multiple *tranches* over a period of time. Moreover, governments often feel compelled to retain a stake in industries considered "strategic", possibly in order to prevent a takeover by foreign investors. To this end a share endowed with special powers (a "golden share") is sometimes retained – although this practice is often criticised especially within the EU, as it appears to distort the functioning of capital markets.

Mixed sales – whereby some shares are sold through a SIP and others through a private sale – allow governments to combine the benefits of a private sale with the advantages of a public flotation. This method usually entails the direct sale of the control to a (group of) investor(s), either through a negotiation or a competitive bidding, accompanied by a public offering as a second stage. The public offering of the shares allows governments to promote capital market development, while the direct sale ensures that the privatised company benefits from an infusion of technology and stronger governance structures than would be the case under a more dispersed share holding structure . A third possible component is the placement of some portion of shares with the company employees, as a means of ensuring worker participation.

1.5.5. Conclusion

This project provides an overview of the causes and consequences of the SOE sector reform process. The final question which arises is the following: is the coexistence of private ownership with public control a transient anomaly or a functional pattern of governance? Providing an unanimous answer is difficult but this question is certainly an important avenue for the future research, both on theoretical and empirical sides. For the time being, we conjecture that the pure privatization (the complete transfer of ownership and control to the private sector) appears difficult to achieve and sustain, as several conditions should be met.

2. Dissemination and use

2.1 Introduction

Dissemination of research outputs and policy options is one of the key objective of the implementation plan of the project (WP11) and its aim is to reach the highest number of possible end-users in Europe and around the world with useful guidelines for sound policymaking will allow to maximize the potential impact of the research outputs. Dissemination of the Project's results is therefore achieved using a new instrument and conventional outlets such as the working papers, workshops and conferences.

Particularly relevant to this aim is the ad hoc **web-based facility entitled "Privatization Barometer" (PB)**, the major dissemination instrument of the project, that ensures the wider exposure of the project's result to the international community. PB is the first comprehensive Internet portal focusing on privatization in the European Union, including the first central and eastern European (CEE) accession countries. As a non-profit initiative, all the content – and its regular updates - is available free of charge to any user. Founded in 2004 by Fondazione Eni Enrico Mattei and Fondazione IRI (two independent research institutions) PB has established a unique and independent source for policy analysis of privatization and related issues that is strongly based on objective research. By reporting comprehensive data and information on the historical process and most recent and future trends, PB provides a focal point for an international audience of researchers, analysts, international agencies, governments and policy-makers. PB has been recently selected by the OECD as its primary source of privatization data, and by World Bank for the supply of revenues data for the WB Privatization Database.

Substantial network effects has been already obtained in the dissemination activity of the Project's first year activities by leveraging on the high visibility of PB. Since the launch in July 2004, PB has been widely accessed (145,980 visitors, 560.000 page views, 340 avg. single IP users per day). The breakdown of the first 1.000 registered users shows PB is attracting considerable attention from researchers and academic users, followed by governments, agencies and international organizations. As the access statistics show, most of present PB content is widely accessed and downloaded to be utilized as a fundamental research tool. More particularly, the breakdown of registered users shows that PB is attracting considerable and increasing attention from the media as a primary source of data, information and analysis on privatization. The section of PB dedicated to UPP is targeting a wide audience, providing information on UPP progress in a widely accessible and non-technical language.

A dedicated UPP **Intranet section** is established and maintained. It includes: (i) scientific contents; (ii) publishing all project findings and intermediate scientific outputs; (iii) and to establish links with the partner institutions.

Moreover, an **electronic newsletter** is distributed to a wide list of academics, policy-makers and interested public at large, starting from the start of the project. The e-Newsletter updates readers on the progresses of the Action and contains direct links to the output of the Action, in order to disseminate the results of the project outside the project.

It is envisaged that during the second year some **Working Papers** and a **Policy Paper** have been produced to disseminate the main results of UPP's activities.

Details on the attendance and presentations by project partners at relevant **meetings and third-parties conferences** with policy-makers, stakeholders and the research community, along with the organisation of dedicated **Seminars and Conferences**, are provided below in Section 2 of this Annex.

2.2 Dissemination of knowledge

The knowledge associated with this project has been shared during the second reporting period through the website, newsletter, attendance and presentations by project partners at relevant meetings and direct contact with policy-makers, local stakeholders and the research community. Specific activities which have been are outlined in the table 1 below.

Table 1: Main dissemination activities

Planned/Actual dates	Type	Type of audience	Countries addressed	Size of audience	Partner responsible/ involved
March 2006	Project dedicated section of FEEM website	Research; decision-makers; general public	All Countries	n/a	FEEM
March 2006	Project web site / Project Section on PB Portal	Research; decision-makers; general public and media	All Countries	n/a	FEEM/All Partners
March 2006	Electronic Newsletter	Research; decision-makers	All Countries (mainly EU 25)	1120	FEEM
June 2006	Conference (FP6 – Priority 7 Project Management Conference)	Research	European Countries	n/a	FEEM
June-August 2006	Interviews	Key local decision makers; Experts	Tunisia, Egypt	20	FEEM
July 2006	International Conference on Game Theory	Research	All Countries	200+	UPF
August 2006	Conference (Econometric Society European Meeting)	Research	All Countries	100+	UPF
September 2006	Electronic Newsletter	Research; decision-makers	All Countries (mainly EU 25)	1223	FEEM

November 2006	UPP Thematic Seminar	Research; decision-makers	Italy	70	FEEM, CERGE-EI
December 2006	Workshop (Simposio de Análisis Económico)	Research	Spain	n/a	UPF
January 2007	Presentation at Conference (FEEM Conference on Sustainable Development)	Scientific; decision-makers; key local stakeholder; general public and media	All Countries	340	FEEM, CIFRA
January 2007	Presentation at Conference (Econometric Society Winter Meeting)	Research	All Countries	200+	UPF
February 2007	Conference (EBRD Conference on Partnership between Government and Private Sector)	Scientific; decision-makers	European Countries	300	FEEM
February 2007	Working paper published in FEEM Wp Series 2.07	Research and scientific	All Countries	n/a	UMIL, FEEM
February 15, 16 2007	UPP Intermediate Conference	research, decision-makers, key local stakeholders	All Countries	35	FEEM/All Partners
February 27,28 2007	Conference on "15 anni dopo: Pubblico è meglio"	Research and scientific	Italy	100	UMIL
March-April 2007	Thematic Seminar	Research and scientific	European Countries	n/a	CERGE-EI
April 2007	Electronic Newsletter	Research; decision-makers; general public	All Countries (mainly EU 25)	1200	FEEM
May 2007	Roundtable - Bank Privatization in MEDA Countries	Decision Makers	All Countries	15	FEEM
June 2007	VI Milan European Economy Workshop	Research; decision-makers; general	European Countries	n/a	UMIL

		public			
July 2007	Working Paper presentation in Conference	Research; decision-makers; general public	European Countries	n/a	FEEM, SWP
July 10, 2007	Workshop: "Il Governo Locale azionista: proprietà, controllo, efficienza nei servizi pubblici locali".	Research; decision-makers; general public	Italy	200	FEEM
September 2007	UPP Thematic Seminar	Research; decision-makers; general public	Italy	40-80	FEEM/UPF
September 10, 2007	Participation to the workshop on "Evaluating the performance of Network industries providing services of general interest"	Mainly Professional	EU	100	UMIL
October-December 2007	Working Papers publication in FEEM WP Series	Research	All Countries	n/a	FEEM/All Partners
November 19,20 2007	Workshop on "An alternative to the market"	Mainly Professional	EU	150	UMIL
December 2007	Project paper publication in MCR	Research; decision-makers	Italy	n/a	FEEM
December 18, 2007	Round Table Seminar Series, CERGE-EI	research, decision-makers, key local stakeholders	All Countries	25	CERGE-EI
February 2008	Electronic Newsletter	Research; decision-makers; general public	All Countries (mainly EU 25)	1150	FEEM
February 15, 2008	Participation to the conference on "Esternazionalizzazioni e Privatizzazioni: i	Reaserch and Scientific	Italy	100	UMIL

	fallimenti dello Stato e del mercato"				
May 2008	Working Papers publication in FEEM WP Series	Research	All Countries	n/a	UMIL, FEEM
June 2008	Publication of a project paper in the academic journal *Economic Change and Restructuring*	Research	All Countries	n/a	CERGE-EI
June 5, 2008	Organization and Presentation in the *Workshop on the Political Economy of Democracy*	Research in Economics and Political Sciences	All Countries	36	UPF
June 21, 2008	Participation in the *Social Choice and Welfare International Meeting*	Research	All Countries (mainly EU15)	n/a	UPF
June 26, 2008	UPP Final Conference	Research; decision-makers; key local stakeholders	All Countries	100	FEEM/All Partners
July 18, 2008	Seminar, OstEuropa-Institut, University of Regensburg	Research	All Countries	15	CERGE-EI
August 29, 2008	Presentation in the *European Econometric Society Meeting*	Research	All Countries	n/a	UPF
September 2008	Electronic Newsletter	Research; decision-makers; general public	All Countries (mainly EU 25)	1350	FEEM
September 2008	Publication of a project paper in *Social Choice*	Research; decision-makers	All Countries	n/a	UPF/FEEM

Forthcoming	Publication of a project paper in the academic journal *Economics of Transition*	Research	All Countries	n/a	CERGE-EI
Forthcoming	Publication of a project paper in *Journal of Economic Literature*	Research	All Countries	n/a	CERGE-EI
Forthcoming	Paper publication in *Mathematical Social Science*	researchers, decision-makers	all Countries	n/a	UPF

Details of the dissemination activities

FEEM (partner n°1)

The first and second issue of UPP Electronic Newsletter have been distributed at the start of the Project (March 2006) and after six months (September 2006). The newsletters were disseminated through the existing PB newsletters mailing list on privatization-related issues, a wide list of academics, policy-makers and interested public at large. In addition, FEEM included a UPP presentation in the six-monthly Newsletter (n. 1 of 2006) which were sent to more than 600 institutions in Italy and to around 500 institutions abroad. Until the end of project (February 2008) an update of UPP results will be presented in the upcoming FEEM Newsletters.

FEEM also organised in co-operation with CERGE-EI a **Thematic Seminar** in Milan, in November 2006, dedicated to Ownership and Performance in the Czech Republic (WP5), attended by around 70 researchers and operators and presented by Evzen kocenda and Jan Hanousek from CERGE-EI, Prague.

UPP co-ordinator Bernardo Bortolotti together with senior FEEM researcher Valentina Milella presented the draft paper *"Residual State Ownership and Asset Prices"* produced under WP8 at the **First FEEM Conference** on Sustainable Development, held in Milan the 25-26 January 2007. In February 2007 Prof. Bortolotti presented the above mentioned paper also at the **EBRD Conference** on Partnership between Government and Private Sector held in London.

The publication of working papers produced in the **FEEM Working Paper Series** - due at the end of the project - has been anticipated for the first empirical paper produced under WP6, published in January 2007.

During the whole duration of project implementation FEEM was in charge of developing the **UPP website** within the Privatization Barometer portal (http://www.privatizationbarometer.net/upp), one of the main dissemination instrument of the project which allows to share information and related material among partners and outside the Consortium (See Section 1, 2 and 3 of the Activity Report for further details).

Moreover, in March 2006 a Project Dedicated page was launched in the **FEEM institutional website**. The page is available online at:

http://www.feem.it/Feem/Pub/Programmes/Privatization+Regulation+Antitrust/Activities/200602-UPP.htm

The first and second issue of UPP Electronic Newsletter have been distributed in first reporting period: the first one at the start of the Project (March 2006) in order to make the UPP presentation and the second one after six months (September 2006). The third, fourth and fifth issue of UPP Electronic Newsletter have been sent in the second part of the Project. In addition, the last publication FEEM included a review of the thematic which were presented during the UPP final conference while a continuous update of UPP results were presented in the previous FEEM Newsletters. The newsletters were disseminated through the existing PB newsletters mailing list on privatization-related issues, a wide list of academics, policy-makers and interested public at large. In addition, in the last publication FEEM included a review of the thematic which were presented during the UPP final conference while a continuous update of UPP results were presented in the previous FEEM Newsletters.

UPP co-ordinator Bernardo Bortolotti together with senior FEEM researcher Valentina Milella presented the draft paper *"Residual State Ownership and Asset Prices"* produced under WP8 at the **First FEEM Conference** on Sustainable Development, held in Milan the 25-26 January 2007. In February 2007 Prof. Bortolotti presented the above mentioned paper also at the **EBRD Conference** on Partnership between Government and Private Sector held in London.

FEEM also organised a **roundtable** in Milan, "**Bank Privatization in MEDA countries**", in May 2007, dedicated to banks' privatization in MEDA Countries. Aim of the meeting was to introduce and discuss the preliminary results of the MEDA Workpackage within UPP Project both to local key experts of the area and to key operators of the banking sector (top representatives of two major European Banks such as ABNAmro, Intesa SanPaolo and Unicredit Group) in the form of a roundtable with limited numbers of participants to allow an open discussion on the most specific issues.

In July 2007, FEEM organized a **workshop** in Rome to present some preliminary results of a project paper: "**Government-owned Enterprises in Italy: Some Stylized Facts**". Target of the workshop was widely varied, going from research to general public. Aim of the meeting was to stress the relevance of the so called "municipal capitalism", i.e. of the increasing presence of firms created and owned by local governments in various sectors. These firms are suspected of being ways on the one hand to by-pass constraints set by public finance laws on the municipalities' borrowing ability, and on the other hand to distort competition in sectors where local authorities are in charge of public regulation. The aim of the research is first to identify direct and indirect holdings by central and local governments in large and medium-sized Italian firms. Second, to provide some preliminary evidence on their impact on economic activity, and on their operating and financial performance. The workshop arouse great interest with some articles published in the major newspapers and at the end of the 2007, the paper was accepted to be published in a national economic magazine (Mercato Concorrenza Regole, edited by Il Mulino).

Another occasion to disseminate the results of the UPP project was the **UPP final informing conference**, organized in two distinct parts. The first part of the meeting **"The End of Privatization?"** developed into three sections and it was followed by a final roundtable.

The general aim of this first stage was to develop the theme of privatization in Italy and Europe and to define some bullet points about the features, the causes and the effects of the phenomenon during the last 20 years. A roundtable was organized for the concluding part of the conference. The main topic of the panel discussion "**From privatization to the new State capitalism: the future challenges**" faced with some critical aspects of privatization such as their impact on the financial markets, the role of the governments which are reluctant to abandon the control over privatized companies and the protectionism appeared during the last years, just to mention a few. The roundtable had as ultimate purpose to define some general guidelines considering the whole effects of privatization on the different stakeholder (employers, shareholders, customers and the wide public in general) and to identify the borderline between public and private ownership. The presence of a new protectionism and a new capitalism sets back the big gambles by the private sector on the largest infrastructures. High profile panel has been invited to this roundtable to discuss and give their critical points of view about these matters.

Some working papers have been produced in the **FEEM Working Paper Series**.

UPF (Partner n° 2)

During the first part of the project, UPF team leader Humberto LLavador presented the draft paper "Voting with preferences over margins of victory" in **four highly recognized international conferences**: the 17th International Conference on Game Theory in Stony Brook, New York (July 2006); the 61st Econometric Society European Meeting in Vienna, Austria (August 2006); the XXXI Simposio de Análisis Económico in Oviedo, Spain (December

2006); and the Econometric Society Winter Meeting in Chicago, Illinois (January 2007). In the second period, the paper have been presented in two other international conferences: the Social Choice and Welfare International Meeting in June 2008 and the European Econometric Society Meeting in August 2008. Furthermore, UPF work team organized a workshop on the political economy of democracy where it showed the results achieved by the team within the UPP project.

One another important goal was the great interest in the project's results coming from the research community: UPF team produced the first empirical and theoretical papers and both have been already accepted for publication in refereed international journals: "Delayed privatization" in *Public Choice* and "Voting with Preferences over Margins of Victory" in *Mathematical Social Science*.

UMIL (Partner n°3)

UMIL work team participated to an Italian conference which was an investigation on the shift regarding the public services; the conference was held in Rome in February 2007. Some months later (June 2007), the workpackage organized the VI Milan European Economy Workshop aimed at presenting to a wide audience of academics, researchers and operators the interim research results of WP6 and fostering discussion on consumer utility reform. The results coming from the research of the project were presented in other important workshops in September and November 2007 and at the beginning of 2008. Two of the papers produced by Università di Milano have been published in the FEEM working papers series.

At the **UPP Final Informing Conference**, the work team presented the paper "The Privatization of Services of General Interest in the EU: the Viewpoint of Consumers"

UvA-CIFRA (Partner n° 4)

UvA CIFRA team leader Enrico Perotti participated as discussant to the presentation of the draft paper *"Residual State Ownership and Asset Prices"* (WP8) at the **First FEEM Conference** on Sustainable Development, held in Milan the 25-26 January 2007.

Regarding the second part of the project, the UvA-CIFRA team partner Armin Schwienbacher presented the paper "The political origin of pension funding and State ownership" at the **UPP Final Informing Conference**, held in Milan the 26 June 2008.

IFO (Partner n° 5)

During the first reporting period IFO did not participate to dissemination activities while during the second part the IFO team leader Thiess Buettner presented the paper "Revenue Shocks and Borrowing Restrictions: Fiscal Determinants of Privatization" at the **UPP Final Informing**

Conference, held in Milan the 26 June 2008.

Furthermore, Gernot Nerb showed "The Outcomes of Privatization: an Analysis of the Survey Results", the report coming from a major work of interviews towards 9 selected EU countries (Austria, France, Germany, Greece, Hun-gary, Italy, Poland, Spain, United Kingdom).

SWP (Partner n° 6)

During the first reporting period SWP did not participate to dissemination of knowledge activities. The four case studies have been published only at the conclusion of the project in the UPP section on the SWP-Homepage:
http://www.swpberlin.org/projekte/projekt.php?PHPSESSID=d2ea60b86fd9303324bd774f5ccd469d&id=8932&active=upp&page=-1.

It is planned, that FEEM as WP4 leader will publish two case studies (on the privatization of public health care and on military services) as FEEM Working papers.

CERGE-EI (Partner n° 8)

CERGE-EI participated to the **Thematic Seminar** in Milan, in November 2006, dedicated to Ownership and Performance in the Czech Republic (WP5), attended by around 70 researchers. Another **Seminar** was held in Milan four months later (March 2007), focussed on the the same topics. In December 2007, Evzen kocenda and Jan Hanousek presented their research findings in an other **roundtable seminar** in Prague.

Overall, the two authors have completed three research articles according to the original workpackage specification. All three articles were accepted for publication in leading academic journals. First article is motivated by the ongoing debate among economists and policy makers about the efficiency and distributional effects of different methods and sequencing of privatizations around the world. It is entitled "Effects of Privatization and Ownership in Transition Economies". The article was accepted for publication in the *Journal of Economic Literature* that is the academic scientific journal with the highest impact factor in the field of economics. Second article investigates the effect of corporate divestitures and subsequent privatization on firms' performance. The article is entitled "Divestitures, Privatization and Corporate Performance in Emerging Markets" and it has been accepted for publication in the academic journal *Economics of Transition*. Third article investigates controlling potential of the State over privatized firms and is entitled "Potential of the State to Control Privatized Firms". It has been accepted and published in the academic journal *Economic Change and Restructuring.*

The results of their papers have been presented also during the seminar, host by OstEuropa-Institut (University of Regensburg) and the UPP Final Informing Conference.

UNIPD (Partner n° 9)

During the whole UPP project, UNIPD participated to dissemination of knowledge activities through an internal presentation of their works both in Intermediate Meeting and the Final Informing Conference. General conclusions coming from their researches have contributed to a more comprehensive analysis of the phenomenon and they have been a valid contribution to better understand the other privatization's topics developed by other UPP partners.

During the second reporting period some **Working Papers** and a **Policy Paper** have been produced to disseminate the main results of UPP's activities. The working papers are first published in the FEEM WP Series, posted on the web site (where they are downloadable free of charge) and distributed in paper copies. They are meant as intermediate outputs and their aim is to stimulate the debate and to encourage broader understanding on the themes. In particular the policy paper was delivered at the end of the project to prepare policy advice, based on project's conclusions, which would be distributed to policy makers. Moreover updated publication of the project activities are actively sought in specialised scientific journals and newspapers. This includes local, national and international press.