Four challenges for effective privatization[1]

Prof. JOHN STOURNARAS CHIEF EXECUTIVE OF IOBE
Dr. SPYROS TRAVLOS BUSINESS CONSULTANT

The modernization of public enterprises began the '90s but remained incomplete. Lack of motivation weak management tools, assignment of indirect social policy to public corporations, combined with the shareholder passivity and confusion in supervisory responsibilities between ministries have undermined the modernization effort. Many business plans remained on paper and annual management reports due to lack of positive results focused on justification for deviations from targets.

It is certain that all stakeholders knew exactly what was happening in public companies. Excess employment, administrative price moderation, inefficient operations, and many other weaknesses were commonly accepted in the post dictatorship era. The system had to offer something for everyone. But the cost of managing this "Agreement" escalated and became unbearable fueling both the deficit and the debt.

Successive governments have been forced to rescue more than once some of the most loss making public companies moving marginally within European Union legislation with incredible ingenuity and hidden forms of aid. Hellenic Shipyards, Olympic Airways, Railway Organisation and defense industries have become for every government in the last 20 years a constant threat.

The distortions in competition with the permanent and not transient financial support of non-sustainable activities inhibited any attempt for economic restructuring and adjustment to new conditions and created a pervasive perception of conservative entrenchment.

The equity offerings in the late 90s began to change behaviours. Governments and trade unions have adjusted to a new savoir vivre. At least, there was greater transparency in balance sheets, partly on procurement and to some extent in labour relations. But the continued protection from competition in several markets led to a containment of the adaptation effort. After initial successes, inactivity returned with vengeance.

The long delays in the privatization process at least allow us to learn from the experience of others: not to repeat the same mistakes and to improve the outcome. There are quite few recorded failures in the global economy in the 30 years since the time that Mrs. Thatcher opened the public sector to market forces. But the development of entrepreneurship in new sectors, coupled with improvements in supervision, yielded considerable results for the rejuvenation of capitalism and created new opportunities for investment and rapid introduction of innovations with tangible benefits for consumers.

---

[1] The article has been published in the daily economic newspaper "IMERISIA" on the 29th April 2011 in Greek under the title "five keys for effective privatisations". This is a liberal translation in English of the original.

The delays can lead the political system to either complete inertia or accelerate the accumulation of proactive forces resulting in a transgression. Let us hope that the second tendency will dominate over the first, as was the case in the '90s, and will motivate many social, technocratic and political forces that support the task of reform. The ruling party, with its heavy ideological baggage carried since the time in opposition, initially trapped in a sterile negation of reforms in general and especially privatization. Thus they lost a unique opportunity to shape on time a more socially acceptable form of transformation of the public sector and implement it when they took over the government in 2009.

The government should even now, after eighteen months of delays, start to shape for each economic sector the appropriate market architecture. In those sectors already dominated by competitive forces the state must withdraw completely (e.g. OTE, banks). In those areas, where liberalisation is imminent, the Public Corporations should be privatized at a faster pace and supervision/regulation should be strengthened by both the regulators and the state to ensure the quality of services and the fairness of pricing (Public Power Corporation, Public Gas Corporation, and Hellenic Petroleum). Finally, in service sectors that have not yet been liberalised, the government should introduce new systems of competition and leave room for private investors providing a rigorous framework for the operation of concessions or other formats such as subcontracting of specific transport services (urban transport, railways, airports, ports). Along with privatization, the government should implement a plan for the development of state property by employing different tools (divestiture, concession and development based on business plan, PPPs). The incomplete records of state land do not offer an excuse for the delays in the exploitation of property. Let us begin with property that is already clearly defined with significant growth potential.

There are four challenges to be addressed:
First, it is important to strengthen the regulation in segments opened up to competition especially at a time when the public administration is quantitatively shrinking and is qualitatively impaired. The practice to establish a separate regulator for each market segment should be overcome. The Competition Commission must be converted into a regulator - umbrella, with specialised units per market segment. A Review of the institutional framework of market supervision should be immediately assigned to a group of experienced lawyers which will propose the new architecture of the regulatory system, defining the general principles and mechanisms of regulation of markets. The governance of markets is especially crucial in the areas of utilities and infrastructure to ensure the delivery of public service and to avoid conflict of interest. Eventually, the state through efficient supervision should ensure competition wherever possible and regulation where it is necessary.

Second, it is essential to attract foreign capital and credible managements. Any privatisation that will be based on a simple reduction of state participation is not expected to add new elements to the dynamism of entrepreneurship and will not result in significant long-term revenue for the Treasury. At this stage strategic options for the future of entire sectors of the economy is under consideration in an international environment dominated by most powerful business groups. Hence, it is of paramount importance to attract reliable investors which will improve the conditions of accession of Greek corporations in the international division of labor.

Third, privatization should act as a catalyst of growth in sectors and areas where state owned companies are dominant. Each privatisation is an opportunity to test practices that have been successfully introduced in other European countries. In transport instead of adopting proven solutions already delivering results in other EU countries, the government promotes "hybrid" models, with the State maintaining its absolute dominance and limiting reforms to a reduction of labour costs and increasing ticket prices, while discouraging the entry of private investment. At a time that Germany has granted to private investors 20% of rail traffic volumes, Denmark 25%, and Sweden has procured the 60% of the subsidized routes in Greece the government insists on maintaining the 51% of TPAINOSE under public control. The concessions to private investors result in cost savings ranging from 25% to 30%. In urban transportation the existing system of public control prevails and privatisation is considered as a threat rather than an opportunity.

Fourth, it is imperative that the privatisation processes are completed with transparency, speed and efficiency. The climate in the stock market should not be burdened or to compete in terms of fund raising with private companies already tested by the liquidity crisis. Regarding the privatisation of real estate, the direction should be not simply the transfer of ownership, but the attraction of funds for productive investment. The selection of privatisation consultants and advisors is the first step to initiate the process of privatization. The end result however will be determined by many factors such as clarity of institutional framework, the general feeling of transparent management of the process by establishing a level playing field and the macroeconomic situation.

The privatization can contribute substantially to reduce debt and make it more viable in combination with other tools. But at this juncture, the bar of expectations should be higher. Privatization can contribute to a radical transformation of the productive system with a direct positive impact initially on economic growth and later on employment.