



Privatization to serve economic development

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ABSTRACT

Original Article:

Received 14 Nov 2013

Accepted 21 Dec. 2013

Published 30 Dec 2013

Keywords:

privatization
development
economy
economic development

One of the principles of a dynamic economy and an economic development factor in advanced countries is "privatization". Privatization is a process to assign priorities to market mechanisms and to make them market orientation. It includes a wide continuum that full privatization and restructuring governmental owned firms are in its both extremes. Finding an optimized method to run economic issues is the greatest concern of government. Government oversizing and expansion its intervention in unnecessary issues which increase costs, decrease productivity, establish parallel entities and lead into improper management are, inter alia, difficulties that governments especially in less developed nations are confronting. It caused that governmental officials and economists looked for a solution. In this vein, privatization is raised as the most radical guideline to resolve this problem. Privatization experience by different countries indicates that not only there is no single global approach for privatization but also its successful implementation depends on different conditions with certain requirements. In Islam and in contrary to manmade systems, economy is considered as a tool for human growth and excellence rather than an aim. In Iranian Constitutional Law, economy is emphasized in various articles. In article 44, economical infrastructure is built. Contemplation in implementing article 44 indicates that correct and complete implementation of this article means the construction of national economic growth and development expressway which requires growth and development of other social, cultural, political, administrative, managerial and organizational infrastructures of a healthy social system. In present paper, economic development is defined through contemplating on article 44 of Iranian Constitutional Law and then privatization and its definitions are provided and possible guidelines to execute article 44 are explained.

1.Introduction

Third world countries' tendency to privatization is the result of spatial pressures and propensity toward consistency with global economy rather than their actual emerged need from their economic context. These countries have expectations on privatization such governmental management change to private management that its decisions are fueled by personal interests, replacing politics – based administrative aims by commercial aims and profitability motivation, allocating financial resources to investment based on their efficiency, mitigating the opportunities to exploit advantages by beneficiaries, reducing corruption in running companies, expanding facilities to accelerate economic growth and development. In 1962 and 1963, privatization was introduced as one of the principles of White Revolution while new trend of privatization was started since 1989 in the format of government's economic policies as well as the 1st National economic, social and cultural development. It was approved by the government to achieve such aims as promoting the efficiency of practices, mitigating government intervention in unnecessary economic fields and services, creating economic balance and optimized utilization of national facilities (Khorshid, 2007). Privatization is a trend by which government investigates the possibility of transferring its functions and facilities in any level from public to private sector and it would undertake such assignment if needed. In such case, privatization can have different moods including direct sales of owned units, contributing private sector in a part of the

outlined the inefficiency of public sector paved the ground for revising the extent of governmental intervention in economy so that in Iran, economic regime devised and ratified midterm economic goals in all areas including privatization in the framework of the 1st economic, social cultural development plan (Komeijani, 2003).

Achieving economic development in the meaning of improving life standard is desired for any society and it is an inseparable element of human evolution. In any society, any person looks for his/her ideals improving knowledge and awareness, improving health and treatment, progresses in social, personal and welfare amenities, law governance and building a social environment along with security and discipline. A traditional society believes that development is to release from ignorance and poverty. A developing or developed society wishes higher aims of growth and welfare based on its economic development extent as well as human and material facilities. Economic development discussions were raised in European countries in 17th and 18th centuries. The pressure of industrialization and technological growth in these countries was accompanied by acquiring the market of weak colonial nations and caused the deeper gap between advanced and backward poles in short time and shaping two ranges of countries in the world: advanced (or developed) and backward (or underdeveloped) countries. (Motevaseli, 1994)

2. Theoretical basics and background

2.1. Economic development

Development term was broadly used after World War II. It means progress and moving from traditional to industrial societies. One should distinguish between "economic growth" and "economic development." Economic growth is a quantitative concept while economic development is a qualitative one. Put it simply, economic growth is increase in national production in a given year compared to basic year. Economic development means growth

operations by these institutes and/or designating certain parts of governmental tasks (Gharehbaghian, 1993).

The experience of government inefficient performance in economy and revising privatization in other countries whose movements

along with increase in manufacturing capacities including physical, human and social capacities. In economic development, quantitative growth would achieve and social entities will be also transformed, attitudes will be changes the capacity to exploit current resources will be increased dynamically and constantly and there are new innovations every day. Besides, one can say that the combination of production and relative share of inputs will be also changed in production process. Development is prevalent in the society and it cannot be occurred only in one sector. Production has no clear threshold. However, it is a qualitative phenomenon due to its dependence to human (in contrary to economic growth which is fully quantitative) without any limitation.

2.2. Economic development pursues two main goals

- ✓ Increasing wealth and welfare of people (an poverty elimination)
- ✓ Job creation

Both aims are toward social justice. Glance to economic development differs between developed and underdeveloped nations. In developed countries, the main aim is to increase welfare and amenities of the people while in underdeveloped ones, it is more focused on poverty elimination and increasing social justice.

2.3. Development aims in the view of connoisseurs

- ✓ **Mike Tudaru:** development is multidimensional. It requires radical changes in social structure, people's thinking, financial institutes, inequality mitigation and abstract poverty elimination.
- ✓ **Birnschtein:** attempt to create development is accompanied with a value load. Enthusiasm to overcome poverty and illness as the most prevalent and important human pains are, inter alia, the aims of development.
- ✓ **Dadley Siers:** development is a multidimensional flow and a different orientation by total economic system, social system and people's habits and beliefs.
- ✓ **Peter Donaldson:** development is radical changes in social structure of selections and inputs to realize all social aims. Development continues by public awareness on changes and contribution.
- ✓ **Misra:** as an Indian author, he emphasizes on cultural aspects.
- ✓ **Gonar Mirdal:** development is to get away underdevelopment and to be released from poverty through better planning.
- ✓ **Brogfield:** development is progress toward welfare aims. Development must mitigate inequality. (Griffin, 2003)

2.4. Types of development

- **Social development:** different types of mutual reaction in a given society occur along with civilization development and involves broader field.
- **Cultural development:** it has further value load and emphasizes on immaterial needs of the people. It is more focused on human understanding, cognitive, valued and propensity fields and behaviors than cultural development process to remove developmental improper subcultures.
- **Political development:** since World War II, development is raised to emphasize on the efficiency of governments and replacing traditional behavioral patterns with modern behavioral models; for instance, progress in contributing people in government would expand civil society.

- **Human development:** human development depends on three key indicators: life time, knowledge, dignified subsistence (Motevaseli, 2003).

2.5. Important features of economic development

Incremental

Self – managed and continuance

Self – reliance

Self - sufficiency

2.6. Economic development indices

One can below items as economic development or development level indices:

- ❖ **Per capita income:** it achieves through dividing national income (GDP) on population. This simple and evaluable index in different countries is usually compared to per capita income level in advanced countries. In the past, US\$5000 per capita income was a sign of development while now the minimum per capita income is considered as US\$10000.
- ❖ **Price Purchase Power (PPP):** since per capita income is computed by local prices and price levels for goods and services are not usually the same in different countries, PPP is used in this regard. In this way, the amount of produced goods in each country is multiplied in global prices and after making necessary amendments, GNP and per capita incomes are calculated.
- ❖ **Sustainable Income (GNA, SSD):** attempts to overcome deficiencies of per capita income and paying attention to “sustainable development” instead of “economic development” would lead into sustainable income index computation. In this way, environmental costs in production and economic growth process are also considered in national accounts (either as loss or as improvement in resources and environment). Then, one can achieve the rate of growth and development.
- ❖ **Development combined indices:** since 1980s, some economists proposed combined indices rather than relying upon a single index to measure and compare countries in terms of their economic development. For instance, one can point out a balanced combined index by McGranahan (1973) based on 18 main indices (73 sub-indices).
- ❖ **Human development index (HDI):** it was introduced in 1991 by the United Nations to compute such indicators: real per capita income (based on purchase power index), life expectancy (at birth) and access to education (as a function of adult's literacy and the average of going to school years) (Mirza Amini, 2013).

3. Privatization

The most important infrastructural factor in setting economic development policies is to determine the levels and importance of roles by both public and private sectors in economic transformation process. Therefore, the framework of such fields as well as the weights of each sector should be determined in economic activities before selecting carious development policies. Determining the weight of each sector in relevant activities depends on numerous internal and external factors such as the aims and ideology of the government, global economic conditions and polarizations, the capacities and capabilities of both private and public sectors and economic development degree. One can enforce manufacturer to produce and sell with the minimum price through

privatization and building a competitive environment. The advantage of the private sector is that one can pose pressure on it through competition – not controlling regulations – to manufacture product by the minimum price. It is impossible in governmental structure. Therefore, privatization mitigates the costs and promotes innovation and, consequently, reduces the prices. On the other hand, due to cost pressures, the inflation is controlled and the society will be benefited. However, exportation will be possible since a merchandizes is exportable which is manufactured by competitive prices. (Motalebi Asl, 2006).

Privatization was coined by Webster Encyclopedia in 1983. It brings different meanings to mind. A way to clarify its meaning is to relate it to governmental activities to supply goods and services. Pf Course, using this term to sale the assets of public sector is considered as an explicit phenomenon in 1980s. Different fields of activities, however, are explained for it (Khorshid, 2007).

The main idea in privatization thinking is that it enforces the competition space and system dominating market and private firms to have more efficient performance than public sector. On this basis, numerous definitions, concepts and theories are provided that involve different aspects and aims of privatization (Motevaseli, 1994).

Veljanosky defines privatization as conducting economic activities by private sector or transferring the ownership of assets to private sector (Moradi, 2005).

Financial international institutes and laissez – faire economists believe that government should be convinced only to devise regulations and it should transfer the ownership of industrial profitable companies to private sector.

Privatization is to transfer current government owed firms to private sector .

Privatization is to eliminate public subsidies to private sector .

In privatization process, the main discussion is on how to allocate society's resources. Who or which mechanisms can determine the priorities of allocating society's resources? It is clear that privatization is a movement to assign priority setting to market mechanisms. Hence, market – orientation is the most comprehensive definition on privatization. Accordingly, privatization means not only ownership change but also “to what extent the operation by an economic firm is in the format of discipline by market forces. Such movement is in contrary to dominating mindset in 1960s and 1970s when dominating attendance of the government in production considered a marginal role for market mechanism (Kiani et al., 1994).

Domestic and foreign studies on privatization are as below:

In their study on the impact of privatization of admired companies in Tehran Stock Exchange on their share returns, indicated that privatization has no favored impact on their return and efficiency and the most important reason has been undesired conditions of Iran, lack of proper grounds and technical issue such as share pricing.

In their study on the impact of ownership type on performance (privatization experience in Iran), found that no statistical significant difference was seen between performance before and after privatization based on the financial information of 18 companies which were transferred from public to private sector between 1991 and 2000.

In a research on the relationship between privatization of welfare services and employees' satisfaction in National Iranian Copper Company, found that there is a positive relationship between privatization of welfare services and employees' satisfaction. In the meantime, there is a positive association between employees' educational level and their job position and satisfaction.

In a research titled “devising a proper model to promote and develop privatization” mentioned the most important aspects of privatization which include in terms of importance: global, international, political, legal, institutional and organizational, designing, assigning, economic, managerial and administrative, socio cultural, virtual and techniques. He emphasized that

privatization status quo is improper and of total 1900 scores, aspects and components of privatization have acquired only 576 scores which indicate 70% distance from ideal situation.

In his research on designing the model of assigning public firms with policymaking approach in Iranian petrochemical industry, Mohammadi (2010) studied privatization status quo in Iran and provided a model in which privatization process starts by considering domestic 20 – year outlook document in which Constitutional Law and regulations of five – year socio cultural development programs are mentioned and privatization is determined in line with financial aims of firms or the same minor aims including profitability, productivity, price, competition and public or major aims such as justice, welfare, occupation and environment. Based on these aims, variables as privatization requirement are determined, necessary to be implemented for better execution of privatization process. These variables include: establishing a private monitoring entity for privatization, enhancing stock market, transparency in assignments, creating competitive environment, adopting and modifying laws and regulations and investment security.

Bortoloti et al, (2001) studied financial and operation performance of 31 companies in ITC industry at 25 developed and developing countries between 1981 and 1998 in two seven – year periods. The studied measures were profitability, operational efficiency and investment in three years before and after privatizations. The finding indicated the improvement all measures in privatized companies.

Bubekry and Kast (2003) studied the performance of 16 African companies before and after privatization. These companies were privatized through IPO in 1989 – 1996. Their findings indicated that although there was a huge increase in their investments, a trivial change was seen on their profitability and power.

Aklino and Salavu (2005) studied privatization efficiency in Nigeria in 1978 – 2000. Their findings suggest a growth trend after privatization in terms of ROIs of shareholders and assets in this period.

Naryana (2006) studied the impact of privatization on financial indicators, prices, service quality, equality and the capability to provide services and pointed out the positive impact of privatization on financial indices (creating capital market), price and the capability to provide services.

In a study titled “operational and stock market performance during the privatization of public firms, studied the Spanish privatized companies through IPO between 1990 through 2001 and concluded that privatization has a remarkable impact on efficiency, sales income and employment.

The main reasons of giving importance to private sector in economic activities include:

Laissez-faire mechanism: as potential deficiencies in this field should be removed if this mechanism is admired as the mechanism to allocate resources. However, the government intervenes since it has exclusive and unique information and power and both are the plagues of the market. Prices will be rightly show the value of goods based on inadequacy or abundance of resources and consumers' preferences if the market is transparent and the economy would pass a desired path by rational reaction of private sector.

Private sector threat by government: government's intervention in economy would slow rive sector activities through different ways:

Competition in attracting the resources: the resources of the society are limited and in the competition between government and private sector to attract such resources, the government is winning in most cases. Hence, private sectors activities are decreased which efficiency and performance in private sector in using the resources optimistically is better than government.

Increase in interest rate: increase in governmental expenditures would increase interest rate and decrease investments by private sector. As mentioned, government tries to help increases in private sector investment in different ways such creating economic

infrastructures, modifying market failure cases, supplying general goods, creating demand for goods and services of private sector (Moradi, 2005).

3.1. Differences between private and public sectors

Privatization is considered due to weaknesses and deficiencies of public sector to which the most important one is lack of efficiency. Wherever private sector can operate effectively there is no economic necessity and justification for governmental activities. Government's economic activity can replace private sector operation only when government can allot resources to production better than private sector. Private sector has more impetus to provide consumers with diverse and needed goods and services and market discipline would enforce private sector to create new needs for its own survival, to discover new resources, to invent new production techniques and, finally, to allocate resources through the selection consumers not political pressures. Through privatization and creating competitive motivations, one can improve the efficiency of firms and to allocate the resources better. Therefore, it is highly important to respect competition. Basically, public sector compared to private sector is faced difficulties in producing and supplying the goods and services with better efficiency and effectiveness. In contrary, private sector is able to supply and provide goods and services more efficiently due to competition, management, structures and manpower that all are fully differed from public sector. These differences between both sectors are determined by aims, management, manpower, reporting systems, organizational structure, nature and business status (Barati, 2004).

3.2. Designing a system for privatization

In addition to public management continuance in the incumbency of governmental owned or affiliated factories and institutes (i.e. banks, organs and public organizations), independent systems should be designed which can be able to assign manufacturing practices (i.e. services and goods) to competent management fields by full legal authorities, predetermined goals and schedules, incomes and planned expenditures. To realize such target in our country which does not enjoy efficient and well – established industrial organizations, mechanism and ambiances like Germany, it is too necessary to help the establishment of legal investment associations. Simultaneously, it is necessary to do below initiatives immediately:

- Downsizing public organizations and eliminating administrative department and directorates and making the government as a headquarters for policymaking, planning and guidance.
- Eliminating the steps of issuing permissions and governmental interventions and deregulating investment and manufacturing system and methods in the format of making general systems and spaces for different development comprehensive plans.
- Preventing government and public companies/organization from developing and making new investments or capital increasing. (Rahbar, 1993)

3.3. Privatization in Iran

During several years, Iranian government has played a vital role in economy and one of the reasons of such highlighted role playing is the huge oil and natural gas resources. In fact, relying upon oil incomes, the government has played as the most important investor in the country. After Islamic revolution and leaving the country by investors and the owners of private industries and possessing their assets by the government, the volume of governmental economic activities expanded than before and by the occurrence of the posed

war, such trend was enhanced. However, weak performance of economic firms and their lower efficiency level shaped the idea of privatizing governmental firms. By the end of war and beginning the first domestic economic, social and cultural program, modifications including privatization were considered as a top priority in government's policies.

The main aims of privatization by the government are mentioned as below:

Improving the efficiency of activities

- Mitigating the ownership by the government in unnecessary economic and service operation: building economic balance
- Optimized usage of domestic facilities

In Iran, implementing privatization program started by the Cabinet approval in 1991. In this approval, only assigning governmental shares was clarified and other methods were not mentioned and share selling through stock exchange was emphasized (Barati, 2004).

The limitations of privatization

Experts recommend that it is vital to devise an integrated, well – established and time-consuming privatization plan in developing countries. Since some groups are benefited or lost during privatization. There are limitations in most developing countries which can be categorized as below. However, one can claim that limitations are summarized into two items including political and administrative

3.4. limitations

3.4.1. Political limitations

- Resistance and barriers of bureaucracy
- Disagreements by labor unities and other groups
- Governmental practices such as tax policies, subsidies, etc.
- Extra regulations so that deregulation is necessary before privatization.
- Ideological reasons as well as believing and ideological dependencies
- Political instability

3.4.2. Administrative limitations:

Current limitations in stock exchange and limited capital market in developing countries particularly in executing multilateral private plans

Lack of financial capitals and investors

Special difficulties such unclear asset values, profitability, etc. (Gharehbaghian, 1993).

3.5. Benefits of privatizations

In its studies on over 1200 companies to understand why companies, prefer to privatize their activities, Privatization Institute concluded that there are 10 below potential advantages for privatization:

- More concentration on a certain activity
- Accessibility on global level
- Access to capitals
- Acceleration in acquiring reengineering advantages
- Risk sharing
- Releasing the resources for other aims
- Cash injection to the company
- Controlling and mitigating operational costs
- Access to (non-internal) resources
- Managing hard or uncontrollable tasks

Above points not only show privatization profit in cost mitigation but also in some cases their importance may be more than cost mitigation.

Contemplating the guidelines to implement article 44 of the Constitutional Law

Based on Iranian Constitutional Law, economy is a tool not an aim. In strengthening economic pillars, the principle is to remove human needs in the route of growth, excellence and evolution and it is not simply focused on wealth generation and profitability like other economic systems. In executing article 44 of the Constitutional Law, only privatization and assigning public firms to people should be considered, because that this method of privatization both before and after revolution has brought no positive and fruitful impacts for population and society and even it has posed many negative impacts and it has not aided society's economic growth and development. To this end, implementing article 44 requires overall contribution by people and government in establishing intellectual, theoretical and practical infrastructures in the format of Islamic economy and in paving the ground for growth and promotion opportunities.

The guidelines to implement article 44 of the Constitutional Law: these guidelines are categorized in four socio cultural, structural (economic, political, social, organizational and managerial structures), human, development process and people's contribution.

Socio – cultural aspect: it introduces value and cultural system and development beliefs and, as a result, the definition and institutionalization of intellectual and value systems of development paradigm based on Islamic beliefs and national identity. considers a high importance for national culture and social values in the format of human behavioral motivations and determinants in political and economic development: "when development values are dominating, development realizes and economic development is not possible without such values."

Human aspect: human is the origination of any change and transformation. Without changes in beliefs, visions, wishes and imaginations, economic development and, as a result, dynamic and sustainable development is impossible. Sustainable development needs people who are ready to play a role which finally leads into economic development, sustainable development and both material and spiritual welfare by right understanding of realities in the world.

Structural aspect: identical to any event in the world, dynamic and sustainable development needs proper administrative, organizational, legal, economic and social structures and frameworks. Therefore, the function of governmental officials and policymakers is to pave the ground for implementing article 44 and as the result, dynamic and sustainable development by modifying administrative, organizational, economic, social and political structures (Khorshid, 2007).

4. Privatization and economic development

In the process of privatization contribution in development, some principles should not be ignored. For instance, privatization does not limit to sell governmental assets to opportunists and privatization should create a competitive process and should block the opportunity of any exclusivism. Privatization should take a radical step in making market economic structure dynamic and it should be based on increasing and promoting the efficiency of production factors. On the other hand, government has some obligations; namely, it should support privatization agents so that they can be ready for competitiveness. The government should support them by providing services and facilities to liberalize their structures. Also, the people should be positivism and encourage investors to make them ready for their clear participation in a competitive market. In other words, investors, people and government should pave the ground for economic growth and development through relying upon both internal and external capabilities so that they can be capable players in global

competition arena. In the process of private sector contribution as the driving force of industrial and economic growth through using their own capital and attracting nongovernmental capitals, using human resources optimistically and efficient management, they should play their role in domestic economic and industrial growth to realize government's developmental goals.

Privatization process is fully different in developed and third world countries. In developed nations, organized entities of the *laissez – faire* have a long history. For instance, legal entities with certain frameworks, stock market, investment banks, exchangeable currencies, advanced technologies and skillful workforce are, *inter alia*, the most important tools in rapid assignment of public companies to private sector. More importantly, people trust legal entities with continuous economic policies and relative stability. Therefore, if a decision is taken to designate a company after technical and level assessments, common social values are not in contrary to such assignment. Market and stock markets are considered as an important tool for investment in finance. Labor laws do not deprive employer from managerial and decision making authorities and there is no distrust on seizing investors' assets and properties. Above conditions make possible to implement privatization process with the lowest risk toward economic development and national interests including the interests of both suppliers and consumers. Privatization in the third world countries finds meaning in a set of comprehensive economic development program. Therefore, ignoring dominating conditions on economic system and relying upon usual policies in privatization process in advanced countries would have no result undoubtedly (Motevaseli, 1994).

5. Conclusion

In national level, privatization should be started by relying upon certain strategic aims since many plans are either stopped or deviated from their main route due to lack of clear strategic, pursuable and evaluable aims. Clarified aims should be defined without any conflict, negative intervention and through a coordinated and prioritized attempt. Privatization strategic aims can be in line with economic, social and cultural development of the region and country, eliminating exclusivism and competition expansion, job creation, developing the activities, mitigating current costs of companies and downsizing the government. Privatization does not only mean assigning governmental owned firms to private sector but also it should also cover mentioned aims; otherwise, there will be no difference between public and private institutes. If such aims are not realized, it is better that such unit is still owned by the government since people will be enjoyed its social and economic advantages more effectively. Privatization can be more successful when rules and competition related issues are prioritized and there should be legal environment to prevent abuses of private institutes from exclusive conditions. If we like that all efficiency interests available potentially through privatization are realized, we should assure that privatized markets are competitive.

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