

Lectio Praecursoria: Privatization as a Means to Property Redistribution in Republic of Armenia and in the Russian Federation

Vazgen Arakelyan

The privatization process in Republic of Armenia and in the Russian Federation is the central point of the research. Privatization is popular economics movement in all over the world. Most developed, developing and transitional countries have demonstrated a great interest in privatization. Privatization in Eastern European countries and Newly Independent States that have been established after USSR collapse is proceeding at a high speed. Privatization as fuzzy concept evokes sharp political reactions. It formed a range of ideas and policies, varying from the eminently reasonable to the wildly impractical.

Privatization is the logical starting point of an analysis of the transformation of property relations in a transition economy. This study leads as to better understanding of the advantages and pitfalls of privatization process and its impact on enterprise efficiency. The comparison between Russian and Armenian privatization implementation and post privatization enterprises performance is bringing new ideas in the vast quantity of literature about privatization and property rights transformation. But at the same time it is necessary to regard the privatization process as a whole, i.e. not only as technical procedures of sales (transfers) of assets from the public sector to the private one, but also as a more fundamental process of the emergence of private property and the formation of institutional prerequisites for further development of market environment.

The topic "privatization" was chosen because of its major importance within Armenian and the Russian Federation economies in the 1990-2002s. Indeed, privatization and deregulation have now reached global proportion

with the concepts having been adopted in both developed and developing countries and even in the Eastern bloc, as the grip of Communism is relaxed

This study was conducted to understand when and how privatization works. This question is actual because many transitional countries only began to undertake large-scale privatization in the 1990s. The results of this study should, therefore, will be of interest to investors, government policy makers as well as officials of international agencies, such as the World Bank and the International Monetary Fund, by providing insights on the way privatization works.

Over the last decade, many studies have attempted to explain the extent of variation and the conditions under which privatization programs will be implemented. Most of the research derives its findings from case studies that focus on a particular region or sector. As such, this thesis seeks to fill in the lacuna of understanding about privatization across time in transitional countries. The first question asked deals with the extent of privatization: When and what factors motivate a government to privatize? The second set of related questions addresses the quality or nature of privatization.

Several studies have recently documented a performance improvement of newly privatized firms in transitional countries. These studies have shown that the outcomes of privatization tend to vary with the level of country development. In my study I have been researching the determinants of performance changes in Armenia and Russia. I conjecture that, in order to explain how privatization works in such an environment, I need to account the ongoing economic reforms in transitional countries, such as stock market

and trade liberalization policies, all of which could affect the outcome of privatization.

Most technical assessments classify privatization as a success. But privatization, especially in transitional and developing economies, is seen as fundamentally unfair both in conception and execution, and it is widely and increasingly unpopular. I have studied about the distributional effects of privatization in focal countries, focusing on changes in asset ownership, employment and returns to citizens and access to infrastructure services. I set out a simple framework for assessing the equity (or fairness) and efficiency gained from privatization, and for understanding any trade-off between the two.

The research was made to find out "How does privatization works in case of state property redistribution and what final result it has?"

In this thesis I have studied the goals of privatization and evaluated various methods used to achieve them in different transition settings. The task is not only to summarize the policy lessons of experience to date with privatization of small, medium and large enterprises in transforming socialist economies. It attempts to research the complex and intertwined goals of privatization of various methods used to privatize state enterprises and progress achieved to this date in Russia and in Armenia.

This thesis focuses on the effectiveness and economic impacts of various forms of privatization, their political impacts including their perceived fairness, their political legitimacy, the extent to which they create new decentralized centers of political power, and their contribution toward creating a class of property owners who favor and support continued liberalization and reforms.

The purpose of this thesis is also to contribute to understanding of the impact of the Russian and Armenian privatization process through an empirical investigation of its effects on the performance of industrial enterprises.

It should be highlighted that the study was dealing with privatization mostly within the industrial sector thereby ignoring the highly controversial privatization of the energy and utility sectors.

I can conclude that while privatization may be generally beneficial from the viewpoint of the shareholders, and perhaps the selling state, it

has not proved so from the standpoint of society, or at least from the standpoint of significant groups of generally poor and powerless actors in society. Ordinary citizens did not receive any visible wealth from privatization, in fact that the mass privatization with voucher scheme was made for equal access for all population. That is why this research made in citizens point of view to better understand the reality of the process.

In order to address the central point properly by studying and analyzing the privatization process in focal countries, its problems and benefits, analyze of the above mentioned process in both countries based on the case study, empirical and statistical studies. The main method of this study is analytical cum descriptive, but for different part of study different methods have been used. Both secondary analyses based on previous studies and primary analysis drawing upon first-hand research materials has been pursued. Data from secondary sources have been collected as well. The study has been prepared in empirical manner. As to the former, the study involves working to establish familiarity with each case included in the study. As to research design, first is pursuing theoretical study to have strong knowledge of privatization. Second step is presenting case study research of focal countries privatization policy. Third, once sufficiently achieved, those studies have been put into each other's comparative context to compare aspects of Armenian and the Russian privatization policies. To a suitable extent, the study of the two focal countries supplemented with statistical and other analyses covering further transitional countries.

In the forth chapter of this study also used SWOT (Strengths, Weaknesses, Opportunities, Threats) analysis method. SWOT method divides the general analysis into two subsections. First, internal analysis reveals strengths and weaknesses with the privatized companies, related to management, marketing production process itself and analyzing the external environment gives the business organization the scope of various opportunities and threats existing in the market in general. The SWOT analysis based on systematic and careful collection.

The following have been found in my research:

- First that small scale privatization in both

countries had the best positive result and creates the middle class owners that produce vast majority of countries GDP.

- Main difference between Russian and Armenian voucher privatization in its fashion is the Pro Rata Approach implemented In Armenia. This approach did not make any changes in the final accounts. Then MEBO in Russia was implemented as a dominant method, in Armenia it was counted as a minor privilege to insiders and did not play important role. The final result in both countries spikes for itself. Mass privatization became a very important step, but only the first step towards efficient ownership.
- Despite this overnight change of ownership of thousands of enterprises, little has changed in terms of governance, management or efficiency, clearly not as much as was expected. Massive abuses, running down assets, tax evasion, non payments crisis, corruption and personal enrichment of management at the expense of their companies was the result. The mentality of the management remained the same.
- Russian cash privatization revenues from sales were ridiculously low by international standards since foreigners and other outsiders were effectively excluded from active participation due to political factors and the embryonic state of institutional, legal and regulatory enabling environment. In Armenia major revenues were made in the state budget by cash privatization method in 1998 by means of sale some attractive for foreign investors industrial enterprises and hotels.
- In Russia case-by-case privatization has very controversial result. In Armenia were privatized only few industrial enterprises by that method.

Both Russia and Armenia have made profound progress in their privatization programs, with both positive and negative results. The final conclusion on which country has done better in its transition efforts is left to the population of these countries, and they will use their own criteria for comparison. This study tries to provide some arguments and objective information on which to base these conclusions.

The economic case for privatization in

researched countries was done more in terms of what is wrong with SOE's than as a positive case for privatization and criticizes. In particular "government failure" is not inevitable and countries can be vary markedly in the quality of government and hence the quality of economic decision-making. Thus, reform strategies should be based on the nature and extent of government failures. In particular, the case for privatization in small and poor countries should be particularly weak. Such huge country like Russia could have a grate success in privatization but because of many obstacles and corrupted officials it has also inefficient and weak program. The problem in many of these countries was not political reluctance, but the absence of an adequate infrastructure to support privatization in situations where local buyers have lacked finance and expertise and governments have had to extend protection and subsidies.

The method of privatization seem to be a matter in explaining efficiency improvements, confirming the concerns of those that emphasized earlier on the agency problem: the well-known concern that non-owner managers do not have the same profit motive as owners and are unlikely to operate in the most efficient way assumed in theory. Long documented in industrial countries, the agency problem is seen a new in various ways in the many countries in transition from central planning to competitive markets. Although the evidence is far from clear, the empirical literature does reveal an approximate ordering of superiority. Start-up firms are clearly the best performers, showing the greatest efficiency gains; firms dominated by outsiders, especially with foreign investors involved, generally show good improvement; insider-dominated firms are the least efficient among the newly privatized, with an unclear distinction between the management-dominated and the worker-dominated cases; the least efficient of all are the remaining state-owned enterprises.

The strategy of accelerate privatization emphasis on the rapid elimination of state ownership. It is usually privatization through give away scheme like voucher scheme. The main goals are the equal distribution to all citizens of state assets. In compare with slow sale strategy the main part of state assets gets the insiders, but as the practice shows only for short period then this property concentrates in

hands of criminals and oligarchs. With the rapid and wide property distribution and ownership reform, without creation of institutions ground privatization leads to inflation and poor economic performance.

Privatization in focal countries shows that the role of the government is important in the transition process. A weak government that cannot or does not bother to control the process only provides the chances of opportunistic behavior. Markets do not guide the process towards Pareto optimality because a functioning market does not exist yet. When the legal framework is vague, informal rules become more important. Legal rules were largely ignored and social networks counted more.

Russian and Armenian privatization did not lead to an efficient result. Insider groups were able to secure their positions and financial conglomerates, led by a few oligarchs, took over the earlier state monopoly in the economy. Privatization strengthened the role of informal institutions at the cost of formal legal rules. Privatization made clear that informal social networks among the new elite are powerful, while the formal rules are weak and not respected. It was also a process that rather weakened than strengthened the development towards the rule of law. It proved that the political and economic elite does not show respect to the developing legal system as long as good relations among the elite can supersede the law.

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