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Privatization in Latin America: The good, the ugly and the unfair

Antonio Estache*

The World Bank and ECARES, Université Libre de Bruxelles

Lourdes Trujillo

Universidad de Las Palmas de Gran Canaria

The views expressed here are however our own and should not be attributed to any of the institutions we are affiliated with. This paper builds on Estache and Trujillo (2004).

1. INTRODUCTION

Most casual observers of reform processes in Latin America are likely to quote privatization as one of the pillars of the 1990s reforms in that region. In fact, Latin America has over 30 years of experience with large scale privatization. It started in 1974 with Chile.[1] Mexico and Jamaica followed at some distance when they launched the first phase of their own major privatization programs in the early 1980s.[2] The clearer image of a privatizing Latin America actually dates from the significant effort in Mexico by the Salinas administration in 1988, and from the widely publicized Argentinean reforms started in 1989 by the Menem administration. Bolivia, Brazil, Colombia, El Salvador, Guatemala, Nicaragua, and Panama later followed in the same path during the 1990s contributing to build the image of a privatizing Latin America.

The privatization of agricultural, fishing, manufacturing, oil, gas and mining industries, public and social services, banks, insurance, and other services resulted in the transfer to private operators or the closure of about 1600 public companies in the region. The biggest bang may have been in Mexico where the number of public enterprises shrank from 1,155 to 219 between 1988 and 1994. But the changes were also quite dramatic in the rest of the region. Argentina privatized 115 enterprises between 1990 and 1994, Brazil transferred 119 firms between 1991 and 2001, Jamaica privatized over 200 companies during the 1990s, and Nicaragua eliminated 343 between 1991 and 1998.

The short term cash flows associated with the privatization transactions were important. The policy generated about US$ 175 billion for the region in income between 1990 and 1999. Almost 60% of this revenue was generated by the privatization of infrastructure services and over 10% by the privatization of financial services. But the total revenue was quite concentrated among a few countries. Indeed, about 95% of the 1990s proceeds from privatization accrued to 6 countries: Brazil (40%), Argentina (26%),

[1] From an historical viewpoint, in some of the sectors, this is a return of the assets to the private sector at the end of a century which saw the nationalization of many of the companies started by private investors at the end of last century and at the beginning of this century. This is particularly true for public services. Most railways, power or water companies where in fact private companies during most of the first half of the century in the region.

[2] Note that Thatcher's programs started later in the 1970s and accelerated only after 1983, implying that Chile and Mexico policy choices were not influenced by the British experience.

Mexico (17%), Peru (5%), Colombia (3.5%) and Venezuela (3.5%).[3] The smaller countries generated much less revenue in dollar terms. However, while not significant for the region, for some of them, the revenue payoffs were important in relation to the size of their economy. For instance, while the average proceeds from privatization represented about 2.7% of GDP, for Bolivia and Panama this income was equivalent to over 10% of their GDP.

To get a better sense of the actual importance of the policy changes behind those flows, consider the index of progress in the implementation of privatization policies proposed by Panizza and Lora (2002).[4] The index measures on a scale of 0 to 1 the privatization effort. This effort is itself measured as the cumulative value of the sales and transfers of companies, starting in 1986, as a proportion of GDP in any given year.[5] According to this index and for a sample of 17 Latin American countries, Bolivia made the most of the policy and reached an index of 0.90. The next best performers were Peru, Brazil, Argentina and El Salvador with indices ranging from 0.65 to 0.35.

The diversity in performance across countries illustrated by this index also makes it quite clear that privatization as a policy choice did not spread throughout the region, contrary to what is sometimes argued by the casual observers. Uruguay, Paraguay, Costa Rica, Honduras, Ecuador, and many of the small Caribbean countries, for instance, have indices well below 0.05 as they have not followed the privatization wave—in a few cases

[3] Chile's main revenue was collected between 1974 and 1985 during its first two privatization waves. Note that the Chilean experience is unusual in many ways since the first wave consisted of a return to the original private owners of 377 firms that had been nationalized or acquired by the Allende administration (see Fisher, Gutierrez and Serra (2003)).

[4] This index is one of several they use to track down the key components of the 1990s structural adjustment programs. Others include trade liberalization, tax reform and financial reform.

[5] This index is useful but somewhat misleading. First, countries do not get credit for reforms undertaken before 1986. This means that the index does not provide a good approximation for Chile, for instance. and probably represents an underestimation of the privatization performance measure as suggested by Panizza and Lora. Second, it does not normalize for the initial conditions. Not all states had the same initial level of involvement in the economy to begin with. The same privatization revenue may thus represent very different reform effort levels for two countries with very different initial conditions. Third, it does not normalize for asset values and hence ignores any undervaluation or overvaluation that may have taken place at the beginning of the process. Finally, it does not correct for any changes in the asset value or the payment to or from the government that may have resulted from a renegotiation.

as a result of a referendum—and have generated very little public revenue from this policy.[6]

Even if this policy had not been adopted with equal enthusiasm by all countries, it is useful to take stock of what had been achieved at a time privatization is being rejected by some of the countries that were once its champions. The recent policy reversals or moderations in Argentina, Bolivia, Brazil, Peru or Venezuela have indeed caught the popular attention as much as the privatization efforts had done during the 1990s. The discussions in the media and some policy circles are however not always based on fact. Indeed, emotions tend to rule the debate on privatization in the region. Surveys, such as the one published by Latinbarometro, forcefully demonstrate the growing sense of discomfort with this policy with an almost steady decline in support since 1998. [7] As of 2003, negative views of privatization ranged from 53% in Honduras to 83% in Argentina. On average for the region, two out of three people had a negative view.

The change in support for this policy has generated a large number of studies since 2000 intended to separate facts from emotions to try to explain the increasing concern with this policy among the population, and hence the politicians.[8] This paper summarizes briefly the main lessons from these studies of the Latin American privatization experience. Since the specifics of privatization are much less homogenous than often believed outside of the region, the various country experiences provide many insights on what has been learned over the last 15 years or so as to what works and what does not work with this policy instrument. In particular, this experience shows that it is important to distinguish between the privatization of public services and other industries and services.

The paper is organized as follows. Section 2 provides a brief overview of the initial conditions which were used to justify the decision to privatize in every country and the main forms that privatization took in each country. Section 3 looks at some of the main achievements of these reforms, including the effects on prices, quality, investments,

[6] Note that in each of these countries, there are ongoing privatization programs under discussion. In Uruguay, for instance, there are now private operators in transport and in the water sector, although the bulk of the services remain under the control of the public sector.
[7] These surveys are in sharp contrast with the strong endorsement by the politicians, as well as the majority of the population documented in a 1995 survey reported at a UN conference. See United Nations (1999)
[8] See for instance, Boix (2005), Bonnet et al (2006), Checchi et al. (2005), Graham and Felton (2005), Martimort et Straub (2006)

employment, financial autonomy and public finances. Section 4 focuses on the things that did not work out the way they were expected to work at the time reforms were designed, including the distributional consequences, competition policy failures and some important institutional and governance issues. Section 5 concludes.

2. Why and How did countries "privatize" to begin with?

Since the history of privatization has so often been rewritten for ideological reasons, it may be useful to review some of the basic facts on the initial reasons at the beginning of the reform processes within the countries. The original motivation and expectation of reform can indeed be quite important in assessing the actual evolution of the impact of the policy, as compared to the perceptions of this impact and the evolution of this perception. It can also come in handy in understanding the interactions between objectives, privatization forms and additional complementary policies that have been or should have been taken to fine tune implementation mistakes. It can finally smooth the learning process that comes from the "doing" rather than simply from an academic assessment of the good and the bad of any reform.

The review of the country specific histories is important because, it is sometimes argued, as in Brune and Garrett (2000), that diffusion, i.e. "copycatting," explains privatization better than domestic, political and economic considerations.[9] In other words, irrespective of what local political speeches may have been arguing over the last 15 years or so in the region, the main motive, according to these authors, may have been a less rational response to local concerns than is often argued in these political speeches. Without questioning the validity of this result, it seems difficult to doubt that in many of the countries, significant efforts were allocated to implement reforms that matched local circumstances, local political feasibility constraints, and what were perceived to be local concerns.

The privatization form has to recognize that countries differ in market size, in level of poverty, in ability to bargain with multi-lateral and commercial banks, in level of

[9] It is also often argued that the pressure exerted by Multilateral donor agencies is a driving force but this is also rejected by many econometric studies, for a example and a brief survey of the econometric literature, see Meseguer, C. (2002).

democracy, or in level of corruption. The details of the implementation of the policies seem to show that governments at the time did understand this quite well. However, before getting into the specific motivations as argued by each reforming government, it may be useful to point to an important historical detail. It is sometimes forgotten that Chile's experience, and to some extent Mexico's experience, pre-date the British experience. Indeed, Thatcher's programs started later in the 1970s and accelerated only after 1983. These could not possibly be copycat experiences and this is why this review starts with these cases studies.

Chile. Chile's privatization experience is in fact a series of privatization waves.[10] The first wave was between 1974 and 1978 and focused on over 550 companies. It is notable that it excluded utilities, but included companies that had been nationalized by the Allende administration. It was part of the adoption of the neo-liberal view of the world carried out under the military regime of General Pinochet—this is what most people seem to remember from that experience. The reforms demanded stabilizing the economy and very restrictive fiscal policies. These very restrictive policies in turn demanded large revenues and *generating revenue was hence the main objective of this first wave of privatization.* To achieve these revenue targets, the government offered controlling packages to investors and provided credit (through auctions often) to investors to ease to the constraints imposed by the underdeveloped Chilean capital market.[11]

The second wave of privatization took place between 1984 and 1990. It started with the "re-privatization" of many of the firms that did not perform well in the first privatization wave (mostly in the finance sector). An important component was the sale of the major infrastructure companies (about 30). For infrastructure services, this was done by transforming the firms into public companies and selling the shares gradually. These shares were tradable and these companies were subject to standard commercial auditing procedures. The percentage of private owners increased in all companies quite progressively. For instance, from December 1986 to early 1990, the increase of the private ownership share in ENDESA, an electricity company, was from 30% to 72%.

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[10] For more details, see for instance, Luders, R. (1991) or Galetovic and Sanhieza (2002)

[11] Although there were cases in which the government simply returned the assets to their previous owners, illustrating the market oriented economy.

Institutional investors (such as pension funds) would eventually account for about 25% of the total stocks of privatized utilities, providing a good long term commitment to the financing of the sector. Usually workers of the privatized would get between 5 and 10% of the shares to ensure their political support. In the case of the electricity and telecoms privatization, a small percentage of former civil servants would acquire a large percentage of these shares—this later became a sour point. Since there was a major concern with the high degree of ownership concentration that resulted from the first privatization wave, the declared objective of this second wave of divestiture was *the increased distribution of ownership rather than the maximization of revenue*.

Under the Lagos administration, Chile entered its last wave of privatization with the residual utilities. The main concern of this latest wave has clearly been efficiency as revealed by the concern for the design of the regulatory regime and highly publicized and controversial debate on the issue.[12] This concern is in fact also quite present in the Bachelet administration that took over from the Lagos administration in 2006.

Mexico. Mexico's experience with privatization is just as important historically as it is contemporaneous to British reforms and along with Jamaica, signals the first set of privatization reforms in the 1980s in the region. It is particularly interesting because it involves the sale of an exceptionally large number of firms and was part of the first massive reform of the public sector after the debt crisis. The reforms were quite encompassing sectorally and spread over almost all sectors, with the notable exception of utilities, as was the case under the first wave of reform in Chile. However, the process was slow as the need to build the political support proved to be a demanding task. Started by the De la Madrid administration in the early 1980s, most implementation did not take place before 1988 and ended in 1994 under the Salinas administration. While the search for efficiency was the official motivation, many saw in the massive effort an attempt to create an irreversible change in the role of the public sector in the economy (Ramirez-1994). The Zedillo administration continued the push but was less successful—partly because the assets put on the market were less attractive, and partly because in some of

[12] Galetovic and Sanhieza (2002)

the sectors the government only offered minority shares, as in the case of the Morelos petro-chemical complex, were matters of concern for potential bidders. [13]

The most publicized impact of this latest wave of privatization was achieved in the transport sector when airports, ports and railways infrastructures were successfully restructured and concessioned under wide media coverage. The experience in the road sector was less successful and required a major restructuring that started just before the Fox administration took over. Its implementation has been very gradual and the outcome is not yet obvious. The announced privatization of the crown jewel, the oil sector, is regularly on the agenda and from its sheer market potential, it should be commercially successful if implemented at some point. The sector has been a public monopoly since 1938 and is likely to be a major source of political argument under any administration. A similar concern applies to the power sector. The debates is still very much alive and was one of the hot issues during the 2006 election.

Argentina. Privatization was a key component of the Argentinean stabilization and reform program and part of the push for a new development model.[14] It was in fact being prepared as part of an effort to reform the state under the Alfonsin administration, but really took off under the Menem administration. It is quite remarkable that 50% of the US$23 billion realized between 1990 and 1997 was used to retire public debt although in some cases, the government picked up new debt in the process when it took over the residual debt accrued by some of the public enterprises it was privatizing.

In spite of the unhappiness of the Argentinean Left who had supported him in his 1989 election, privatization gained popular support thanks to very effective marketing of the reforms by the Menem administration, including the distribution of shares to employees as part of the privatization of some of the infrastructure services. In contrast to the experiences of Chile and Mexico, the core of the program was, indeed, the "privatization" of public services and in particular infrastructure services. Over 60 contracts were signed by the national government alone. The relative importance of this sector in the privatization agenda reflected the fact that the fiscal crisis impeded the historical subsidy levels in the sector and hence rationing of service and quality were

[13] La Porta and Lopez-de-Silanes (1999) and Ramirez (1994) for more details on Mexico.
[14] See Estache (2004) for a much more detailed discussion of the Argentinean experience.

starting to become a major issue. But for these sectors, "privatization" was only in name since most of the services were in fact concessioned, that is leased for a specific duration with specific levels of services and investment obligation specified in contracts. In many cases, workers also received a percentage of the income generated by the reform process. This concessioning approach became the model for the region. In Argentina, the commitment to the private sector went beyond the contract, but also included the signature of international treaties with the governments of the main investors (e.g. Spain, Italy, and France) as a way to demonstrate the political commitment to the reforms.

In the other sectors, asset sales took place in a wide range of activities. The most important was the privatization of the state oil company YPF which was a major success and had a major demonstration effect in the region for the sector. But somewhat surprisingly, it was when the Menem administration put market assets on sale such as Argentina's share of the Iguazu Falls—Brazil owns the other share of the zoo— that strong popular reactions against privatization policy started to grow. This unhappiness with the policy accelerated with the recession that resulted from the credit crunch after the Tequila and Asian crisis. There was also a major incident in which parts of Buenos Aires went without electricity for up to 10 days. The De la Rua administration had a difficult relationship with the concessionaires and as the 2002 crisis exploded, the privatization of the public services become a major headline in the local press and among opinion makers, ending the initial support that it had enjoyed at the beginning of the reform process.

The Kirchner administration has revisited the public service concessioning programs early on. Many of the contracts of the 1990s have *de facto* been cancelled or restructured. New local actors, some public but many private are now running many of the services that were under the management of large foreign operators until the 2002 crisis implying a clear sense of pragmatism in the interactions of this government with the private sector.

Bolivia. Faced with the prospect of a complete economic collapse, in 1986 Bolivia became the second country in the region (after Chile), and the first democracy, to implement economic shock therapy under an IMF structural adjustment program. In that context, the formal start of the privatization process started in 1992 with a law that laid out some of the groundwork for the changes to come. Broader structural reforms, however, were left to the administration that took office in 1993. The reforms concentrated on infrastructure and banking. The specific objectives were to attract foreign investment, increase competition and efficiency, and strengthen public finances. Privatization was one of the four major components of the reforms—the others were modernization of the legal framework, establishment of independent regulatory systems, and restructuring of the relevant Ministries. The privatization was primarily through a new approach called “capitalization” which generated 80% of the USD 2 billion revenues from privatization. This approach allowed strategic investors, selected through a public competitive bidding process, to obtain a 50% controlling stake in the enterprise. However, instead of purchasing existing shares from GOB, the winner invests the bid amount in the enterprise, as an increase in capital, within a fixed period of time. This approach was used in cases where substantial additional investment was desired, as it ensured new resources. Concessions or simple sales were used in other cases.

Politically, the approach also had strong appeal because the government was not actually selling its assets, but rather inviting the private sector to make new investments, and because the population would share directly in the eventual profits of the companies. The main drawback from a macro stabilization viewpoint was that the resources were not going to the Treasury. However, at the time, the government saw this as a benefit since it was trying to minimize the risk of additional revenues that could lead to an unsustainable expansion in expenditures. The privatization efforts of the residual public services slowed down significantly after the widely publicized incidents in Cochabamba, in 2000, where a water concession turned sour. [15]

As Kirchner has done in Argentina, the Morales administration has renegotiated many of the contracts, including a very mediatic reversal of the privatization of hydrocarbons implemented in 1996 by then president Sanchez de Lozada. For all practical purposes, many of the privatizations implemented a few years earlier are for now on hold.

Brazil. The Brazilian privatization program started in 1991 under the Collor administration and was continued by the Cardoso government and ended up being one of

[15] See Barja and Urquiola (2003) for a much more detailed discussion of the Bolivian experience.

the largest worldwide in dollar terms, outside of the programs adopted in Eastern Europe. It worked quite well until 1998 when it slowed down as the economy turned sluggish. The program has now been placed on hold by the Lula administration. Between 1991 and 2002, it transferred over 120 companies to the private sector. An interesting feature is that many companies were not transferred with majority stakes, but under minority stakes — that is without management control—suggesting that the size of this market is large enough to get investors interested to take part even without control.

Implementation was simultaneous at the national and subnational level, particularly in Sao Paulo. In both cases, the main purposes were to generate revenue and cut outstanding public debt. In dollar terms, the transactions resulted in over USD 100 billion of net revenue. The privatisation of infrastructure services, mostly telecoms, roads, railways and electricity generated almost three quarter of the income. The other companies included many research institutes, councils, and other professional organizations which had historically been organized as autonomous public companies and had been restructured during most of the 1980s. While in dollar terms this was a very significant privatisation experience, in terms of its impact on the structure of the economy the real impact remains unclear. Some of the historical industrial champions of the country are now in private hands, as well as important sectors such as telecoms and railways. However, there are still many sectors for which liberalization and competition are much more important concerns for the government and where the public sector continues to be the major player. This includes ports, the oil industry, and many components of the energy industry and of the financial sector.[16]

Lula's administration has been much less enthusiastic about the privatization option than the Cardozo administration but has not imposed any significant policy reversals. Lula’s team has publicly acknowledged the successes of many of the privatizations and has made it clear that it will not renationalize companies that were sold. They are unlikely to implement more however. The new policy is to champion public-private partnerships rather than any sale of assets.

Colombia. The decision to privatise in Colombia was actively considered as early as 1986 when the government started to work on the divestiture program of the former

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[16] See Macedo (2000) or Pinheiro (1996) for a more detailed discussion on Brazil

Instituto de Fomento Industrial, which covered a large share of the manufacturing capacity of the country and had historically been the engine behind the industrialization process of the country. At that time, the privatisation policy was essentially viewed as an instrument to promote efficiency. The implementation of the program accelerated as part of a liberalization program initiated in the early 1990s, but at that point, its revenue effect became a major concern of the government, along with the desire to attract foreign private investment. The agenda was modest since historically, the size of the state had been relatively modest for the region. However, the revenue objectives were important for the government and contributed significantly to the 1994-98 stabilization program.

Concession and sales contracts were the main instruments used and the constitution and legal systems were changed to facilitate their usage. Concession contracts were intended to be used mainly for public services. Between 1993 and 1998, 35 concession contracts had been signed, most of them for roads, gas pipelines, and telecoms services. In spite of needs in over 1,400 municipalities, few contracts were signed in the water and sanitation sector. As for the other sectors, local, regional, and the national governments, during the same period, only 25 transactions took place in which shares were sold to private investors. Most of the deals took place in the manufacturing and mining sectors. Overall, the achievements of the 1990s have been relatively modest and since then, support to the program has been subject to major swings. Most of the effort has been and continues to be on the restructuring of sectors to promote competition wherever possible. [17]

The short term future looks much more pro-privatization than in many of the other countries of the region. President Uribe indeed introduced a plethora of neoliberal reforms since assuming office in 2002, including an interest in scaling up the privatization efforts. In addition, the government of President Alvaro Uribe has budgeted for the privatization of more than 280 government-owned enterprises, including partially-privatize the state-owned oil company Ecopetrol.

Jamaica. The privatisation experience in Jamaica is really the tale of the reversal of a nationalization policy carried out between 1972 and 1979 by the Manley government. During the Manley tenure, this government had created 185 public

[17] For a detailed discussion of this experience, see Combo and Ramirez (2002)

companies covering all infrastructure and most banking and tourism services. As in many countries in the Caribbean, this nationalization policy was a rejection of private multinationals. This rejection was reversed through after election of Seaga in 1981, who campaigned for the return of private capital in the country. In other words, privatisation was initially adopted on ideological grounds. It was not until 1985 however that the privatisation program took off seriously. The catalyser was an emerging fiscal crisis for which revenue was needed and the program started with the offering of public shares in a major bank.

In a surprising turn of events, Manley, the father of nationalization 20 years earlier, was elected again in 1991 and decided to extend the privatisation experience. The main objective was now to reduce the size of the state and promote full scale liberalization to improve efficiency in the economy. The main policy action on the privatisation front was a further decrease in the government shares combined with an increase in the share of employees in the ownership to over 10%. After that stage, the government was only a minority owner in most companies. In phase 3, the government sold its residual shares through a local investment syndicate.

Within 10 years, Jamaica had privatised 201 companies across all economic sectors. By 2000, considerable progress had been made across the board, in particular in the financial sector. Four state-owned banks and a number of smaller entities were merged into the Union Bank, and restructuring of the National Commercial Bank continued with both banks being prepared for privatization. Following some setbacks—when some privatized entities reverted to public ownership or continued needing government subsidies—privatization has generally enjoyed strong support until very recently.[18]

Nicaragua. Privatization in Nicaragua took place in a very different context, somewhat similar to the Chilean context when it reversed the Allende nationalizations. The election of Chamorro was a rejection of the socialist model, which in turn resulted in the first phase of privatizations between 1991 and 1996. Privatizations included a wide range of very different sectors across the production line, from agriculture to services, including banking, but excluding utilities. Infrastructure privatizations were at the core of

[18] For more details on the Jamaican experience, see Paredes (2003)

a second wave of privatization started in 1995, during which electricity and telecoms were restructured and their services concessioned. Between 1995 and 2002, this wave generated close to 5% of GDP in revenues, and residual reforms are still under way. [19]

The main criticism of the first phase was a lack of transparency regarding the fiscal payoffs from privatization; these were quite important given that they reached 2.5% of GDP every year during much of the initial reform phase. Some of these revenues were used to wipe out the commercial debt of the privatized companies, but the rest went into complex budgetary accounting settlements. In recent years, the privatization efforts have significantly cooled down and including a very intense public debate on the privatization of the water sector. The newly elected president, Daniel Ortega has however stated that he would maintain the economic policies enacted since he left office, including the privatization of formerly state-owned businesses.

Panama. Started in 1992, the privatization program in Panama has largely been concluded. It cut across sectors and started with the sale of a state cement company and a state-owned fruit company. Within 4 years, the government had awarded concessions for private toll roads, cellular phone service, railways services, and ports. Intel, the Panamanian telephone company, was partially (49%) sold in mid-1997 and is now being managed by the British firm, Cable and Wireless. Government-owned casinos and race tracks were privatized in 1998. The power company was restructured and converted into eight companies, which were partially sold to the private sector in August 1998. Four American companies participated including Enron, Coastal, AES and Constellation. Two sugar mills were privatized in 1998 to local groups with some Colombian participation. Pending announced privatizations include a large convention center and the international airport. Water privatization was halted in 1998 after violent protests and appears unlikely to proceed under the current government.

Although there had been substantial new foreign investment in recent years, most of it resulting from privatization, the implementation of the policy slowed dramatically in 2000, as opportunities and enthusiasm for further privatization dwindled. Instances of questionable government practices have soured some large international firms on doing

[19] For a detailed discussion of the Nicaragua experience, see Freije and Rivas (2002)

business in Panama. These include past bidding procedures, contract obligations, project security, and a slow and imperfect judicial system.

The position towards the private sector is unlikely much in the foreseeable future but processes and social concerns are taking a much higher profile as in many other parts of the region. President Torrijos was elected in 2004 on a platform which included a commitment to increase transparency and to address the social concerns associated with the privatization of the public services, most importantly water which has been associated with very strong protest from a significant part of the population. [20]

Peru. After its worst macroeconomic crisis, Peru launched, as part of a macroeconomic adjustment program, the reform of its public enterprises under the Fujimori administration. The sector covered all activities from agriculture, mining, industry, public services to banking and was widely viewed as unfocused, costly and inefficient. The design of the program was intended to attract foreign private investors to the extent possible. Most of the privatization took the form of sales with about 5% of the revenue generated through concessions and a few capitalizations deals. The program was initially modest and focused on 23 companies that were all sold within the first 2 years. The peak of the program was during the 1994-1996 period when 64 more companies were privatized including the telecoms and energy companies. In 1998, the program started to cover the transport sector and enjoyed mixed success. In its first decade, with the privatization of about 150 firms, the program generated about USD 8.9 billion in revenue and investment commitments of over USD 7 billion. Over 80% of the revenue was generated by telecoms, electricity and mining. While the telecoms and banking sectors have in fact been fully privatized, the main residual assets of the government that have not yet transferred to the private sector are in infrastructure and agriculture.[21]

The acceleration of the privatization of these residual companies was part of the initial agenda of the Toledo administration to generate enough revenue to cover a growing deficit problem. Instead, the program slowed down significantly and in electricity, the government was in fact forced to reverse the privatization of two companies in 2002. Alan Garcia, elected president in 2006, is likely to have to address

[20] For more details, see the web site of the Government of Panama (http://www.state.gov/e/eb/ifd/2005/42100.htm)
[21] See Torero and Pasco-Font (2003) for a detailed discussion of the reforms in Peru.

the pressure of a changing public opinion in the region, including a strong resistance to further privatization, in particular in politically sensitive sectors such as the water sector.

Summing up. This overview of selected country experiences suggests that:

- Privatization has been used to address multiple objectives
- Privatization is a much too generic word which hides a multiplicity of concepts and instruments
- The privatization of infrastructure services should be addressed as a separate category.

These three lessons are reviewed next in some detail.

The objectives. The brief overview of country experiences shows that there were many different objectives to the reforms. There are certainly many ways of categorizing these objectives, whether explicit or implicit; one way is to classify them into the following 7 types:

- ***Ideology,*** a conscious attempt to redefine the boundaries of the role of the state in the economy; this was clearly the case in Mexico, Jamaica, Nicaragua or Chile.
- ***Fiscal pragmatism,*** or the decision to rely on the sale or lease of public assets to contribute to the fiscal effort needed to implement a stabilization program. This was the case in the first wave of privatization in most countries and was a strong motivation for privatizing the transport sector, which historically has imposed a heavy burden on the public sector-- most obviously in Argentina, Panama or Peru, but also in Chile, and at least implicitly in almost all cases.
- ***The improvement of the performance*** of a sector through changes in incentives and a focus on the commercial objectives only, rather than the multiple objectives typically assigned to the managers of public enterprise. This may have been the dominant motivation in many of the privatizations in Brazil, Chile, Colombia and the second stages of reform in Jamaica; this is one of the reasons why restructuring to facilitate competition in and for the market is often the first stage of any privatization.
- ***Increasing the access to private financing*** was a major consideration in the reform of major public service in all countries.
- *The* ***dissemination of ownership*** of productive assets in the economy, to push intra-market competition was quite clearly the case in Brazil, Chile and Colombia.

- ***The development of the local capital market,*** as in the case of Bolivia in particular, but in many of the other countries such as Argentina, Bolivia, Chile, Jamaica or Nicaragua where workers were given shares of the companies privatized.
- ***The restitution of recently nationalized assets*** as in the case of Chile and Nicaragua at the end of the Allende and Sandinista governments respectively. [22]

Whether these objectives were explicit or implicit is not all that important. As we will discuss later, the weight assigned to the various objectives was probably a more important determinant of the outcomes.

One size privatization does not fit all. No two countries in the region have followed exactly the same model—in spite of the fact that advice and consulting on privatization and restructuring by former government officials have become major exports products for Argentina and Chile! The differences in initial conditions contribute to explain the choices—Argentina, Bolivia, and Peru were in the midst of a macro crisis and had little bargaining power. This was not the case for Brazil or Mexico, who worked at their own speed and enjoyed strong bargaining power. The differences across countries in the weight assigned to each goal also drove the differences in approaches to privatization.

The categorization of the approach to privatization is itself a challenge. There are indeed many ways in which the term "privatization" has been used in Latin America. One way is to classify privatization is into the following five different approaches:

- ***Full Sale/divestiture:*** this is when the public sector gives up all control and ownership. In Latin America, it has been most common in competitive industries such as telecoms or power generation for infrastructure, most agricultural and fisheries sectors, and service sectors such as insurance or banking; Mexico provides a large sample of privatizations that followed this model.
- ***Sale of majority or minority shares***; this approach allows the government to retain a certain level of control, to co-share the gains or losses achieved by the private operators and to follow a gradual approach in the implementation of the reform; this control can vary on a wide scale.

[22] For an interesting discussion of the trade-offs between ideology and pragmatism, see Manzetti (1999)

- ***Lease/concession:*** this is now the most common approach for infrastructure services and has the main political advantage of allowing the government to retain the legal ownership of the assets; the relationship with the private sector is through a contract which specifies the rights and obligations of all parties involved; Argentina is widely perceived to be the poster boy of this approach, but concession contracts are widely used in the region across countries for infrastructure privatizations.
- ***Capitalization and other forms of development of the capital market***: This approach allows the government to catalyze the development or expansion of a capital market which in many of the countries has proven (and continues) to be one of the major impediments to sustained growth. This is particularly the case for sectors requiring long term investment with politically difficult pricing options, as in the case of public services. Vouchers programs and the allocation of shares to the employees were widely viewed as a potentially important "buy-ins" for the unions into a new more capitalist development model, but its effectiveness was modest at best.
- ***Restitution***: This approach was, for obvious reasons, specific to the few countries in which political changes had resulted in large nationalization programs. The form of restitution did however vary across countries and generally matched the more standard privatization program.

Why is infrastructure privatization special? The country surveys show that infrastructure services tend to be taken into consideration in a particular way. The countries which implemented privatization in a state of crisis (e.g. Argentina, Bolivia or Peru) had placed the "privatization" of infrastructure at the core of their initial reform wave, while the countries in a position of strength took their time (e.g. Brazil, Chile and Mexico). This gives a sense that infrastructure is politically special and that when governments have the choice, they seem to prefer to leave it for last, but that when they have a major concern, the fiscal burden imposed by the sector leaves them with little choice and forces governments to take on the public pressure associated with the privatization of public services.

The perception that infrastructure is special and especially difficult, politically, is indeed widespread. Many users feel entitled to the key public services. Water is widely recognized as a necessity— electricity and public transportation are about to reach that status—and it seems that cell phones are close to being in the same category for the new generation of users. The idea of passing on control to the private sector of these basic necessities is typically a source of concern when this control is combined with a right to recover costs to minimize the subsidy requirements. This is why even if the de facto control of the sector of many public services was often shifted to the private sector as part of the reform process, the adoption of concession contracts by reforming governments was so popular for this sector. It allowed governments to manage the political perception of the privatization process, at least initially (see Table 1).

Assets were not sold, but leased, and in many cases were expected to generate revenue for the government. The only infrastructure sectors where privatizations with ownership change took place were in the telecoms and power generation sectors. These were major sources of revenue during the 1990s in the region. For most infrastructure services however, the most notable fact was not necessarily the revenue generated or the reduction in the associated fiscal cost, but the fact that privatization was taking place in the context of a major restructuring aimed at promoting competition. For many, this was the main signal of a commitment to the neo-liberal policies now questioned in the region.

Table 1: Relative importance of Concessions Contracts in Infrastructure Privatization in Latin America 1990--2000

Sector	**Concession as a % of Total Infrastructure Privatization Projects**
WATER	89%
TRANSPORT	97.5%
ENERGY	54.4%
TELECOM	0.5%
TOTAL	**65.5%**

Source: World Bank PPI Database

This questioning however is not happening in a neutral context. Over the last few years, in particular since a series of international crisis have hurt the region, unemployment has returned and poverty levels have increased. A few major crisis such as power outages and water rationing problems—due more to climatic condition than to the privatization policy—is modifying the perception of a large share of the population on the benefits of such reform. Infrastructure concessions are now widely viewed as equivalent to any other type of privatization and hence questionable in this changing environment. Indeed, as the economic and social situation of many households deteriorated, and as many were facing difficulties to pay their bills, their interface with the private operators ended up being similar to interactions they would have with car dealers or bankers. This was in sharp contrast with the treatment they had received from the public operators of public services when non-recovery of bills would simply be transformed into new demands for subsidies or transfers from the public sector accounts.

In sum, infrastructure is special because it seems to be at the core of changing perceptions on the desirability of reform. Failures in this sector will drive the overall perception and it is thus crucial, to the extent possible, to distinguish between the effectiveness of privatization in infrastructure sectors and privatization in other sectors. Drawing general conclusions from analysis of privatization ignoring the political, social and economic characteristics of infrastructures and the associated services would be misleading. This can be clearly seen in Checchi et al. (2005) who find that disagreement with privatization is most likely when the policy involved a high proportion of public services as water and electricity.[23]

3. HOW EFFECTIVELY DID PRIVATIZATIONS POLICIES MEET THEIR OBJECTIVES?

Ignoring for now the ideology motive for privatization, it seems useful to assess the extent to which the objectives have been met. This should give a clear sense of the "good" achieved by that policy—although this does obviously not apply to the ideological goal. This section offers a review of these achievements relying on a large body of recent literature.[24] Whenever possible the discussion points to the differences in achievement between infrastructure "privatizations" and others since they seem to shape some of the negative perceptions of privatization in the region. The review focuses on fiscal, performance and quality effects of the reforms.

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[23] They also find a strong negative when the respondent is poor, privatization was large and quick. High inequality of incomes also mattered.

[24] Chong and Lopez de Silanes (2004) offer a useful overview for a large sample of countries but fail to distinguish between the privatization of infrastructure activities and others. Andres et al (2005) offer an overview of the empirical evidence on the effect of privatization in infrastructure, offering important refinements of the conclusions drawn by Chong and Lopes-de-Silanes (2004)

In terms of the fiscal objectives associated with stabilization programs, these seem to have prevailed as one of the most important, if not the most important, objective and the immediate—i.e. the short term—impact of reform was quite positive. In the 1990s, in 18 Latin American states, accumulated privatization revenues averaged a sizeable 6 % of GDP (IADB, 2002); additionally, debt restructuring allowed reductions in interest rate charges and debt amortization schedules. In contrast to other regions (again, outside the OECD states), over half of all Latin American privatizations have been high value infrastructure or utility firms. From 1990 to 2005, private investment in infrastructure alone in Latin America totaled USD 416 billion, almost the double of the investment achieved by the attractive East Asia-Pacific region. These sorts of figures had to look good in the books in the short run.

But this is only part of the fiscal story. The cross-country studies generally ignore that fiscal gains come in two forms: a stock effect and a flow effect. The numbers usually quoted give a sense of the stock effect (this is what the gains from the sale or the lease tend to pick up). However, there is also a flow effect (the demand for operational or capital subsidies) which can and does change over time with demand, with renegotiations, and with financial restructurings aimed at assisting the poorest performers. What appears to be an initial gain from the stock effect can easily become a loss from the accumulation of negative fiscal flows effects. Renegotiations of concession contracts throughout the region are generating a risk of a major shift back of investment responsibilities towards the public sector, which would thus offset the initial gains. This observation is particularly important in the context of infrastructure services where contracts renegotiation often lead to reduction in private sector commitment to investment and increases in government commitments to subsidies.

In terms of the impact on the performance of the privatized firms, in general, the success is quite difficult to deny in general terms. The most analytically rigorous studies of Argentina, Chile, Colombia, Mexico and Peru—many done by Latin American academics— show that the performance of the privatized companies has improved in terms of profitability (measured as return on sales), operational efficiency (measured as sales per workers) and output.[25] As compared to the pre-privatization situation,

[25] IDB (2002)

profitability across the board increased as follows: 61% in Mexico, 51% in Argentina, 41% in Peru, 10% in Colombia, 8% in Brazil and Chile, and 5.3% in Bolivia (although in this case, it was measured for a smaller sample). These results are of course impressive, but it is unfortunate that the studies do not distinguish between regulated and competitive sectors. The only study to do so systematically is for Chile, making the case for additional analysis of this difference across countries.[26] Indeed, they find that for competitive firms, there are no major changes in efficiency as a result of major restructuring programs. Most of the gains in profitability from privatization are in fact due to improvement in the regulated sectors that mostly cover the infrastructure services.[27]

The discussion of the operational gains, measured in terms of sales per workers, is somewhat complex. Indeed, it is often argued that the main efficiency gains from privatization come from the resulting reduction in employment. Could it be that the 88%, 92%, and 112% gains achieved by Chile, Mexico, and Peru respectively are mostly due to job losses in those sectors? The fact that the output of the privatized firms increased in these countries by 25%, 53%, and 25% respectively suggests that not all gains must have come from cutting employment, although it is hard to deny the employment reductions in the short run. In Argentina, for instance, employment decreased by 40% in the privatized firms.

One dimension often omitted from the discussions on the literature and in public policy debates is the impact of the reforms on the quality of the goods and services provided.[28] In many cases, and in particular in the case of infrastructure, privatization was associated not only with improvements in production, allocation, and technological efficiency, but also with major improvements in the quality of service offered.[29] Few today seem to remember the five to ten year waiting period to get a residential and sometimes a commercial phone, the interminable delays in obtaining repairs and services,

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[26] Fisher, R., R. Gutierrez and P. Serra (2003)

[27] According to that study, the gains are due to improvements to operational efficiency stimulated by effective regulatory regimes. This conclusion is however not unanimous in Chile, but the surrounding debate will be discussed later. The main question not answered by the study is the extent to which this increase in the return has been excessive or consistent with a normal return for these assets.

[28] Ramamurti (1998) is a notable exception since he documents improvements in quality in transport and telecoms as a result of Latin American Reforms.

[29] For a survey of the improvements in efficiency, see Estache, Guasch and Trujillo (2003).

and the high costs of bribes paid to utility officials to jump the line and obtain—and maintain—connections. In many of these countries, few remember that the lack of safety and reliability of public transportation strongly contributed to the increase in the use of private transportation modes. It is in that context that many of the reforms were initially welcomed except by the public sector workers (and their families) who lost jobs, and often associated privileges; jobs and privileges that were financed by taxes paid by the contemporary population, or bonds currently being repaid by the following generation.

In sum, it seems that the standards applied to assess the effects of reform today are significantly higher than the standards used to gauge delivery systems under which people were living with at the beginning of the 1990s in Latin America. This may be one of the reasons why the conclusions that emerge from these quantitative results, even if they point to some potential problems, are in sharp contrast with the unhappiness with the effects from privatization expressed in surveys of impressions. The issues raised in the next section contribute to solve part of the puzzle.

4. SO, WHAT ARE THE REALLY UGLY FACTS ASSOCIATED WITH PRIVATIZATION?

There are many issues that have emerged from this experience that deserve being highlighted in this overview. The rest of this section is a brief annoted list of these problems and supporting bibliographical references.

The continued and growing fiscal cost problems. Many, if not most, observers of the reforms would argue that fiscal objectives were dominant in most countries. Any failure on this count would then be a major set back for the policymakers who implemented them. However, most of the literature has focused on the stock problem, which seems to have been reasonably well addressed by the reforms. When adding the flow problem alluded to earlier, the picture is not as clearly positive. There is indeed increasing anecdotal and analytical evidence that the flow problem has not been solved. Campos et al. (2003) showed that for the infrastructure sector over the long run, Latin America's private participation in the utilities sectors tended to reduce the demand for recurrent subsidies and increased public investment in the sector. The exact opposite was found for transport privatisation: private transport investments crowds out public investment in the sector, but requires a commitment to operational subsidies. In other words, privatizations have been associated with increases in either recurrent or investment public expenditures overtime. The net effect of the stock and the flow effects are an empirical matter which needs to be assessed at the country level. This analysis is overdue.

The observed rates of return. In countries where privatization took place in non-competitive activities, a fairer assessment of the performance would also monitor the match between the cost of capital and the rate of return. Privatizations were not intended to create or recreate rents for private operators. In a recent paper on the infrastructure sector, Sirtaine et al. (2005) show that depending on how costs are classified, as a revenue or as a cost, the rate of return on capital can vary from 9% to 33% in any given sector. Considering that the cost of capital varied between 15% and 25% for most sectors of most of the countries, it is clearly not very easy to assess how much the regulatory regime mattered and how big of a rent was actually created by the reform process.

The underestimation of regulation of the residual public services monopolies. This is related to the rate of return discussion and is particularly important for infrastructure services. A key reason for infrastructure privatization's lack of popularity is a feeling that the documented efficiency gains achieved by privatisation have not been distributed fairly. Estache (2004) shows for Argentina that the major efficiency gains have not been shared with the users as expected in many of the key sectors. This is to a large extent the responsibility of the regulators or of the design of the processes firms have to follow. The principal distributional mandate of regulators is to assess the cost reductions achieved by the operators and to pass on some—a fair proportion— of these gains to the consumers as part of the scheduled tariff revisions processes. In too many countries, the regulators may be too weak (that is, captured by politicians and/or operators) or may simply be incompetent to deliver on this mandate. The basic efficiency gains that should eventually be shared have typically not been measured by the regulators and hence seldom redistributed.[30] In sum, regulators are crucial players in determining the perception of the equity of privatization because they largely determine the extent to

[30] To be more precise they are distributed from the government, politicians and the managers of the public enterprises to a new combination which includes now includes, the government, politicians, the private managers and the shareholders of the privatized regulated services. Consumers, as a group, only get a share of the cost savings in the form of tariff reductions if the regulators are good and fair.

which the poor get their fair share of the gains from reform (if they are working with proper legislation).

Chisari et al. (1999) document the regressive consequences of poor regulation in the context of privatization and regulation of energy, telecommunications, and water sectors in Argentina. The analysis separates the benefits of privatization per se, from the benefits of effective regulation. The finding is that privatization yielded operational gains in the infrastructure sectors equivalent to 0.90 percent of GDP, or 41 percent of the average expenditure on utility services. Effective regulation added gains worth 0.35 percent of GDP, or 16 percent of the average expenditure on utility services. Higher income households gained more in absolute terms than lower income households, but the benefits of effective regulation as a proportion of existing expenditures on utility services were highest for the lowest income quintiles. This is because regulation acts as a mechanism for transferring rents from the owners of capital to the consumers of the service. Overall, according to the simulations, income inequality drops significantly if regulation is effective.

The painful employment and wage effects. What seems to stick to the memory of people is that they lost their job as part of the privatization process. In many cases, the number of people who lost their jobs was significant at the company level (as high as 70%). This number, however, seldom represented more than 2% of the total labour force in each country—with the exception maybe of Nicaragua where the adjustment was quite dramatic. Moreover, over time, employment recovered in many of these industries. Chong and Lopez-de Silanes (2003) show that for a large sample of Latin American firms 44% of the firms that fired workers before privatization re-hired the same workers about 18 months later. In Peru, in the telecom sector (Torero, 2002), or in Mexico (Estache et alt., 2002), in the port sector, the evidence is quite strong that with increased demand private operators recruited heavily What this suggests is that while in the short run job losses are a problem, in the medium term, they are driven by macroeconomic conditions and not privatisation. For instance, in Argentina, a recent paper by Benitez et al. (2003) shows that credit rationing following the Tequila and Asian crisis could be blamed for most of the increase in the unemployment between 1994 and 2000. These types of analyses are however largely ignored by the media-driven debate.

The mismanagement of the social costs of reform. McKenzie and Mookherjee (2003) suggest that in spite of what is widely argued regarding privatisation in Latin America, there is no clear pattern in the direction of price changes. In fact, prices went down 50% in 5 country studies conducted (Argentina, Bolivia, Mexico, Nicaragua and Peru). Moreover, they point out that when prices rose, this negative effect was offset by a corresponding increase in access to goods and services previously not available. An almost simultaneous research project, managed by Ugaz and Waddams Price (2003), on the social impacts of the reforms shows that in many cases the price increases were most painful for the poorest and that this was often mismanaged by the authorities; tariff rebalancing and reforms aimed at improving efficiency resulted in regressive tariff structures. One of the most highly publicized cases was the Cochabamba water concession in Bolivia (where 70% of the people live below the poverty line).

Because this case may have catalyzed many of the massive rejections for large private operators in the region, it is important to understand its underpinnings. The social and hence political problems began when subsidies were eliminated and the price of water was tripled in January 2000. This hurt the utility’s existing customers, but also peasants (largely Quechua Indians) who would have to pay for water that previously had been available free of charge. The price increases in Cochabamba were partly due to improved cost recovery through reductions in subsidies, but they were also necessary to pay for a USD 300 million project involving the construction of a dam, a tunnel, and water purification plants that would boost water supplies to the Cochabamba area. Soon after the April 2000 protests, the private operator pulled out of Bolivia and the government of Bolivia repealed its water privatization legislation. Following the departure of International Water, the management of SEMAPA was turned over to its employees and the citizens of Cochabamba. Bechtel has since sued the government of Bolivia, asking to be reimbursed for the approximately USD 25 million in investments it has made to date. Water privatization efforts have never been the same since then, in Latin America, or elsewhere in the developing world.

The increased regressive taxation of privatized services. An underestimated source of unfairly distributed outcomes from reform is the transformation of the public service sector into a major source of tax revenue for all government levels. When they were operated by the public sector, infrastructure services sometimes generated large revenue volumes for the government level responsible for the operation of the service (even though this was often not enough to cover all costs). After privatization, at least in the case of utilities—but not always in transport—it seems that these sectors are becoming net “cash cows” for all the government at all levels. In Argentina for instance, utilities generate about 1 percent of tax revenue for all levels of government, mostly from a 35 percent income tax and a 21 percent VAT passed on to consumers. But the effective tax rate paid by users is typically much larger than 21 percent because of municipal and provincial taxes. The indirect taxes on telecoms and electricity can add up to over 55 percent of the cost of service in some large municipalities. This is why when assessing the impact of reform on tariffs, it is quite important to look at the evolution of tariffs with and without taxes. This is also important in undertaking international tariff comparisons for similar services since tax burdens vary across countries. The failure to distinguish between the evolution of tariffs with and without taxes distorts the assessments of the effects of reform. The experience suggests that there are an increasing number of situations where private operators are effectively sharing achieved efficiency gains with the government rather with the users. This may be appropriate, but not when done through a regressive tax system.

The high rates and high profiles of renegotiation. One of the most surprising events associated with privatization was the commonality of renegotiations of contracts in the public service sector. Table 2 shows that one in three contracts were renegotiated in Latin America and that rate goes as high as one in two for the transport sector, and three in four for the water sector. Renegotiations took place on average 2.19 years after the award of the contract; this average is for concessions granted for about 20 to 30 years that had a five year period for a tariff review (for concessions granted under a price cap regime). Essentially, in two out of every three contracts, the change is requested by the operator. This is a significant proportion which raises many questions on the consistency of the government over time to the commitments made when reforms were initiated. In many instances, the renegotiation result in higher tariffs, lower investments, and/or lower service quality. Whether the renegotiation is justified or not is not that important from the viewpoint of the public— the main concern is that the effects of the revision tends to be on the users or on the taxpayers.[31]

Table 2: Incidence of Renegotiated Concession Contracts According to Sectors and Characteristics

All infrastructure sectors %	Transport %	Water %
30	**54.7**	**74.4**

Source: Guasch (2004)

The illusion of competition for the market. To some extent the fact that governments are forced to get into a renegotiation is the result of the fact that there were often few bidders when they auctioned the businesses. This points to the failure of efforts to achieve competition for markets where simply opening up competition in the market was not possible. If competition for the market is to be effective, the number of bidders participating in every auction should be significant and the nature of the bids should be such that there is no concern about risks of collusion. If there are not enough local bidders, opening the doors to foreign bidders can only help. One of the failures of reforms was that this competition was seldom as effective as expected. In many cases, there much fewer bidders than expected. This is particularly true for the privatization of infrastructure services. The evidence available suggests that competition for the market is not working well in most developing countries and that increased trade in services may be helping but not much. Typically the number of serious bidders for a concession or a greenfield project in the infrastructure sector is not much higher than two or three—there are some examples with more players, but this is not the norm. Technically, this is competition, of course, but not impressively strong competition. Moreover, in many cases, the new foreign players are associated with the local players who enjoyed most of the procurement contracts awarded by these companies when they were public.

The high concentration of players in some markets.[32] Part of the explanation for the limited number of bidders is the limited number of players, at least in some of the

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[31] In many instances, the request for renegotiations are consistent with the terms of the contracts or with the regulatory regime, but these are legalistic considerations the users and the opinion makers do not often get into, partly because the details of the contractual arrangements are not public or partly because they react strongly to their exclusion from the implementation of the reform process.

[32] See Benitez and Estache (2005) for a discussion of the problem at a global level

markets. In the transport sector where the construction component continues to be important for roads, ports and airports at least, companies such as Dragados (Spain), EGIS Projects or Bouygues (France), Macquaries (Australia), and Bechtel introduce competition in many parts of the world. This does not seem to be enough to ensure that every auction attracts the interest of many bidders. The major railways and ports contracts around the world are shared by less than ten companies, the power and telecoms markets have a somewhat larger number of players but not much more. The extreme example in supply concentration is the international “sanitation” privatization business (water, sanitation and solid waste). Between 1990 and 1997, out of 58 projects involving about USD 25 billion in investment and covered by the PPI database, 28 were awarded to Suez-Lyonnaise des Eaux, 13 to Vivendi, 6 to Aguas de Barcelona, 6 to Thames Water and 5 to SAUR International. This suggests 5 major players on the supply side. Even when there are significant opportunities for competition, market concentration continues to be strong. For instance, there are close to 100 “significant” independent power companies who can compete for IPPs. However, the top seven concentrate about 50% of their equity in projects (AES, National Power, Southern Energy, Edison Mission Energy, Tractebel, Sithe Energies, NRG Energy and Enron Intn’l). Similar observations hold in the other sectors. There are not that many foreign banks or insurance companies in Latin America, nor are there that many active players in the mining or oil sectors. Ultimately, this raises local frustration with the perception that the governments are being sold out to “bad” multinational companies, while in practice, it raises supra national competition issues which cannot be dealt with individually by national governments.

In sum, this section suggests that there are lingering problems associated with the use of privatization as a policy instrument in Latin America. However, many of the flaws and problems which have been blamed on privatization have very little to do with privatization. They reflect poor preparation of deals, misunderstanding of key social, economic and political constraints which have to be addressed as part of any reform and which maybe underestimated by the privatization teams, in particular those working on infrastructure deals.

6. CONCLUDING COMMENTS

Latin America's privatization seems to have delivered a lot more good than is currently recognized by critics. Overall, the evidence is quite strong although not always as strong as the most dogmatic partisans of privatization keep arguing.. The degree of success, has varied quite significantly across sectors and across countries. So did the number of ugly facts that deserve consideration in this assessment of the Latin American privatization experience.

The main differentiation of performance is probably between the privatization of competitive and non-competitive activities. While the privatization of competitive industries has gone relatively well in the region, it has not enjoyed the same success for non-competitive activities. The regulation of non-competitive activities has indeed proven to be a major challenge for most reforming governments. Whether voluntarily or not, the experience of infrastructure privatization shows that for many of the regulated firms, the rates of return have often tended to be much larger than the cost of capital their operators or owners were facing in most sectors. Moreover, the major efficiency gains achieved from privatization have been slow to trickle down to users. When users are foreigners, because the output is exported and demand is inelastic, there is no local complaining, particularly since often part of rent will stay in the country through royalties or tax contributions. When the non-competitive industries in question cover the public services for which demand is not very elastic and that many people consider an entitlement, the diagnostic is different and the perception of ugliness increases. In spite of the major improvements in service quality and access often achieved, the failure to pass efficiency gains through tariff cuts, in light of the often high rates of returns in regulated sectors, have been a source of conflict between users and operators.

The main problem across the region has been the weaknesses of competition and regulatory institutions put in place as part of the reforms. The commitment to strong agencies has been the exception rather than the rule and in general competition agencies have proven to be much more effective than the regulatory agencies. This has been and continues to be an issue. Ultimately, the governments have either failed to understand that bad regulation is just as regressive as the indirect specific taxes that all government levels have been imposing on regulated services, or they have implicitly decide to collude with the operators, since the higher profits also mean higher tax revenue. Since consultation processes have tended to be just as weak as regulatory processes, the voices of the users have seldom made it to the decision making process.

While the ultimate assessment of the effectiveness of privatization needs to balance the good and the ugly, it is important to recognize that assessments can also be unfair in that they ignore the relative importance of many factors that have little or nothing to do with privatization as a policy. In many instances, the privatizations were only one of many policy changes taking places. Various international financial crises quite dramatically hurt the investment opportunities for many of the new operators. Local banking reforms that did not always work out contributed to the problem. Non-existent, non-performing, or only nascent safety nets contributed to the pain of adjustments associated with short term employment reductions and price increases. Decentralization also often allowed sub-national governments to offset some of the benefits to users of the reform achieved by the national governments—e.g. offsetting price reductions with local tax increases. Finally, in many countries, politicians involved in the reforms are now being accused of corruption and of accruing private benefits from the reforms. These emerging corruption cases are the result of flawed consultation processes. Corruption is also a key reason for the rejection of a policy which many people assess on the bases of associated processes rather than on the bases of outcomes.[33] Full scale assessments need to isolate these factors if they have any claim at being fair. Only then will the analysts be able to come up with a true sense of the good and the ugly associated with the privatization policy in the region

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