ABSTRACT

Most of the work on privatization in Eastern Europe to date has concentrated on the change of ownership issue and its importance for the restructuring process. In our previous papers, we have linked these issues to a broader question of the future corporate governance structure in Eastern Europe. But all of the studies so far have looked at the impact of privatization primarily in terms of its effect on each enterprise taken as a unit. The aggregate effects of privatization have usually been left out of account, presumably on the assumption that the interaction among firms and the effect of their restructuring on the economy as a whole had no particular bearing on the appropriate method and scope of privatization to be pursued on the enterprise level.

In this paper, we begin to fill this gap in the literature, and link the discussion of the various approaches to large-scale privatization with other problems of economic transition, such as the absence of a general infrastructure of the capitalist economy (the banking system and capital markets) and the state of the existing capital stock that may make a large portion of the post-communist enterprises nonviable in a competitive environment.

One of the informational constraints under which the East European reformers operate is the absence of any reliable knowledge as to what percentage of the capital stock of their countries is hopelessly obsolete or otherwise nonviable. In this context, a rapid and effective method of privatization, introducing true competition and genuinely hard budget constraints in Eastern Europe, may lead to a string of bankruptcies and to levels of unemployment that none of the countries involved, without the cushion of enormous transfers from the West, would be able to afford. In order to deal with this problem, our analysis of privatization encompasses not only issues related to corporate governance structure, but also the relation between privatization plans and the information concerning the quality of available capital stock and the aggregate effects of microeconomic reform. This leads to a reformulation of our approach to mass privatization and novel conclusions regarding the appropriate speed of privatization.