PRIVATISATION: A WIDER PERSPECTIVE

Mescal Stephens
Manager, Strategic Policy
Department of Transport
Nedlands
WESTERN AUSTRALIA

Anne Nolan
Principal Policy officer
Department of Transport
Nedlands
WESTERN AUSTRALIA

ABSTRACT: *Underlying the current popularity of privatisation as a panacea for our woes is the perception that most things the public sector does, the private sector could do better. This belief tends to be based on the strength of theoretical economic factors such as profit maximisation. This paper, therefore, commences with an examination of privatisation from an economic perspective. In doing so, it reviews the concept of privatisation, its theoretical appeal as well as recent privatisation experience, with particular emphasis on the transport and communication sector. However, it is readily apparent that privatisation, its objectives and role, is a more complex issue, involving the interrelationship of politics, history, organisational theory, management, psychology, and even international trade, as well as economics.*

Privatisation is one of a number of policy responses available to improve the efficiency and effectiveness of public sector organisations. However, the privatisation debate needs to be cognisant of the wider arena in which the issue is based and to question its real objectives. This paper therefore concludes that privatisation should only proceed with caution, as its foundations are not theoretically strong, nor its practical consequences unambiguous.

Introduction

The transport sector of the economy features strongly in discussion on privatisation, deregulation and corporatisation. Transport encompasses the whole spectrum of private through to government ownership as well as close regulatory control to virtually no economic regulation. The factors which have led to particular services being provided by government are often now largely historical. However, the existing structure and dichotomy between public and private can not, in the future, be considered to be immutable. The current topical nature of discussion and debate on privatisation is significant, in our opinion, in that it has the potential to raise many questions and focus attention on whether the community is best served by the present economic and organisational arrangements or if more beneficial structures can be developed.

The argument on privatisation generally has been couched in economic terms; the organisational theorist is on comparatively low ground as organisational theory has tended not to concentrate too much on comparisons between public and private sector performance. The aim of this paper is to illuminate the economic arguments by the flickering light of organisational theory. Consequently, the basic proposition of the pro-privatisation argument that most things the public sector does the private sector could do better is addressed from both an economic and organisational perspective.

The purpose of this paper is to draw attention to the fact that the efficiency and effectiveness with which organisations carry out their business is a substantially more complex issue than that implied by the simple distinction between 'private' and 'public' ownership. Consequently, the underlying theme of this paper is that privatisation per se is not as significant an issue as current discussion would indicate. Indeed, it has tended to become an umbrella term to shield from discussion the question of just who are the winners and the losers, that is, some discussion of net public benefit.

There is a need to define terms used in discussion of privatisation to avoid confusion regarding the basic issues and premises involved. Therefore, this paper commences by examining two central terms: privatisation and efficiency.

1. Setting the Scene

1.1 Privatisation

Usage of the term 'privatisation' varies considerably. It is used to cover a range of different policy options involving the relationship between the government and private sectors. Trengrove (1986, p.5) suggests "The use of the word has now been expanded .... to encompass almost any measure which involves expansion of decentralised and individual, as against political and bureaucratic control and decision-making".

Kay, Mayer and Thompson (1986) distinguish between three different strands of policy on privatisation:

* transfer of ownership of assets to the private sector, i.e. denationalisation;

* liberalisation or deregulation - the promotion of competition or competitive behaviour, in certain activities which are either reserved to statutory monopoly, or subject to restricted entry; and

* tendering - the contracting-out of public provision to private firms.

In this paper, however, usage of the term privatisation is confined solely to the issue of transfer of ownership of assets to the private sector. It is maintained that transfer of ownership to the private sector, the literal interpretation of privatisation, is a separate and distinct issue to that of deregulation or the contracting of services. Privatisation does not imply deregulation and, in fact, may result in increased or new forms of regulation, particularly of monopoly enterprises. For example, in the case of British Telecom, privatisation led to the creation of a new regulatory authority. Likewise, deregulation does not necessarily imply the transfer of ownership to the private sector. The regulatory aspects governing a particular activity and ownership are different concepts. Investigation of privatisation, however, does have implications for deregulation and contracting out of services, particularly their relative ability to contribute towards increased efficiency. It is likely that confusion over what privatisation actually is has contributed to some of the exaggerated claims regarding its benefits.

This concentration on privatisation as an ownership issue is also justified by the fact that the overwhelming attention both in the United Kingdom and elsewhere has been on the policy of denationalisation. Moreover, the transfer of ownership implied by denationalisation is probably the most politically controversial aspect of methods designed ostensibly to increase efficiency of the public sector.

1.2 Efficiency

Given the apparent pre-eminent emphasis placed on the efficiency gains to be achieved from privatisation, exploration of the meaning of efficiency in both the economic and organisational jargon is also warranted. Economic efficiency has two aspects:

- productive efficiency relates to the use of resources to produce goods and services at least cost

- allocative efficiency relates to the allocation of resources among alternative uses to produce goods and services that the public wants.

Allocative efficiency refers to total resource allocation. Optimal allocative efficiency is achieved when it is not possible to change the existing allocation of resources in such a way that someone is made better off and no one worse off.* The key to the fulfilment of this condition is that prices should generally reflect the marginal cost of production. If the price of a commodity does not equal its marginal cost, then price will not accurately reflect the cost of increasing or decreasing output by an additional unit and will, therefore, fail to display the appropriate signal to purchase/produce the optimal quantity. Marginal cost pricing provides consumers with as much information as possible about the resource allocation effects of their consumption decisions.

Under a perfectly competitive system where firms maximise profit and consumers maximise satisfaction or utility, individual self-interest ensures that firms and individuals act unwittingly to fulfil the conditions for allocative efficiency.**

The presence of increasing returns to scale, externalities, imperfect information and public goods, however, provide classic examples of situations where the market system does not achieve economic efficiency. That is, there is market failure. Public intervention or public production therefore can be seen as a legitimate response to market failure.

1.3 Privatisation, Efficiency and Market Failure

Privatisation, by itself, will not ensure allocative efficiency. The substitution of protected private monopolies over public ones, for example, may not improve allocative efficiency. Private monopolies are unlikely to adopt marginal cost pricing as it is in the power of monopolies to charge prices above marginal costs. The difficulties involved in implementing the theoretical guidelines established for pricing and investment for either public or private enterprises are well known. For instance, a series of White Papers from the United Kingdom on improving the performance of nationalised industry based on economic guidelines have not had a significant impact on the actions of these organisations.

Productive efficiency essentially requires minimisation of costs. It is with productive efficiency and the power of market discipline that arguments for privatisation rest most strongly and this will be discussed at length. The difference between maximum effectiveness in the utilisation of inputs (productive) and the actual effectiveness has been termed by Leibenstein (1976) as the degree of X-inefficiency.

---

* This is the so-called Pareto criterion for optimal allocation of resources. It requires that the marginal rate of substitution of goods by consumers to be equal and these in turn must be equal to the marginal rates of product transformation of firms which must be equal to one another. Efficiency in production is a necessary prerequisite, of course, for allocative efficiency.

** Another aspect of efficiency which is not specifically accounted for in this static model is dynamic efficiency. Long-run dynamic efficiency can be said to be occurring when the economy is expanding along an optimal growth path at a rate which reflects a socially accepted distribution of consumption between present and future generations.

Hence, there is a positive role for government intervention in a market economy based on economic considerations, that is, due to market imperfections. The role of government is further indicated if society has objectives other than just economic efficiency, in particular social or income redistribution goals and objectives.

1.4 The Australian Response

In Australia, the common response to perceived market imperfections, including those caused by considerations of equity, is to have recourse to public production. Thus investment in the Commonwealth's sixteen largest enterprise holdings had a book value of $12.3 billion as at the end of June 1986. The scale of this investment and the reform of the public sector has been the object of considerable recent scrutiny through a series of government papers. It is noteworthy that, in two of them, Statutory Authorities and Government Business Enterprises (1986) and Policy Guidelines for Commonwealth Statutory Authorities and Government Business Enterprises (1987), clear reference is made to the intrusion of ideology into the argument. The assumptions that an enterprise will deliver services more efficiently if it is privately owned or that private ownership is synonymous with competition have no more validity than an assumption that, because an enterprise is publicly owned, its resources are necessarily being deployed in a manner which will maximise the public benefit [Policy Guidelines (1987, p. 2) and also Statutory Authorities (1986, p. 2)].

Indeed, the aim of 'maximisation of public benefit' is not a new concept and, in Australia, there evolved in the 1880s the statutory corporation - specifically railways and savings banks - as a deviant administrative form administered by experts and removed from ministerial departments with this purpose. They were within the ambit of Government in the first instance because the few private railway jointstock companies in the 1850s proved inefficient and unequal to the task of opening up communication networks. As public assistance was increased to these companies, government nominees were added to the boards until State acquisition. Both railways and savings banks developed the Weberian bureaucratic characteristics (see later discussion) as a new form of management in ways which are now regarded as orthodox, namely a professional permanent head, clear lines of authority and merit recruitment. Since the 1880s, Australian debate has not been neglectful of the alternatives and, even at that date, there were suggestions that the railways should be handed back to private enterprise. Since then, both Liberal and Labor Federal Governments have argued at various times for State entry into as well as out of business. The philosophy of public enterprise which has emerged has therefore been essentially non-socialist. Some of the great contributions to Australian public enterprise were made by the later Menzies' Government.

Wettenhall (1987) has argued that the predominant feature of the Australian discourse on State enterprises is pragmatism. While there may be occasional triumphs for those who would diminish the threat posed by the leviathan state - notably when Labor adopts an extreme nationalist position - at this point, as always, there has been a continual search for innovative public enterprise policy which is moderate in effect and usually incremental in implementation. There is probably more to the argument than economics alone and, at the risk of mystification, Wettenall speculates that public enterprise probably made its debut with the public works performed by 'government servants' with the aid of convict labour. He (p. 2) refers to the special pragmatic quality of Australian public enterprise as emerging from the 'marriage of ideological reluctance and economic necessity'.

2. Private Ownership

The transfer of ownership to the private sector or public enterprises is justified by those in favour of privatisation on the basis that it will increase efficiency both in an allocative and productive sense.

For instance, Hartley (1986, p. 19) states "transferable property rights will encourage the pursuit of profits and hence the search for ways of reducing production costs or producing more valued outputs". Clarke and Porter (1982, p. 51) argue "The profit motive, and the system of accountability based on property rights which underlies it are vital for a dynamic economic system whose output is tailored to the demands of individual consumers". Similarly, Beesley and Littlechild (1983, p. 4) claim "Privatisation will generate benefits for consumers because privately-owned companies have a greater incentive to produce goods and services in the quantity and variety which consumers prefer. Companies which succeed in discovering and meeting consumer needs make profits and grow; the less successful wither and die. The discipline of the capital market accentuates this process: access to additional resources for growth depends on previously-demonstrated ability".

The following examines the strength of the underlying argument for privatisation which is based on the role played by the profit motive, bankruptcy and takeovers.

2.1 The Profit Motive

The underlying theme in these quotes is that self-interest in the pursuit of profit motive will result in the most efficient outcome. While it is unwise to discount the influence of the profit motive entirely, it is not as predominant as these economists would like to believe.

There is a good deal of theory on motivation that argues that people are propelled by factors other than profit. Simon (1957), March and Simon (1958) and Cyert and March (1963) argue that administrative human beings do not maximise but satisfice because there are cognitive limits to human choice. Indeed, the limitations of rationality and problem-solving processes are seen as determining the basic features of organisational structure. Hence, economic man is replaced by administrative man. Coming at this from another angle, nearly all motivational theory puts 'self-actualisation', that is, some notion of fulfilment in some sort of higher plane, as the highest motivating force. This is especially the case with senior public servants who are more motivated by intrinsic job satisfaction such as community service than their private sector counterparts who are more motivated by extrinsic satisfactions such as a high salary [Cacciope and Mock (1987)].

Economics is not concerned with the management processes. However, management theory is vitally concerned with the management processes that will lead to superior performance. Most people will be familiar with a recent best seller "In Search of Excellence" [Peters and Waterman (1982)] and its espoused rubrics which do not appear to have stood the test of time. It is not surprising that, in the literature on organisational effectiveness, there is no agreement on what constitutes excellence or how you achieve it. "Consensus regarding the best, or sufficient, set of indicators of effectiveness is impossible to obtain" [Cameron (1986 p. 541)]*. Individuals in organisations may prefer contradictory aims such as growth and stability, efficiency and flexibility, high capital investment and high returns to stockholders, autonomy and control, and so on. Effectiveness is a multidimensional construct so that single indicators such as satisfaction, morale, turnover, or return on investment are unlikely to assess it.

The economic argument has it that, if a firm pursues profit maximisation, it will prosper. Child (1974) investigated the factors leading to differentials in performance in 82 British companies. He found that nearly all the chief executives, of high and low performing firms alike, gave a very high priority to net profit over the long term, that is, five years, but also gave equal weight to achieving a high rate of growth. Hence, the pursuit of profit and growth did not necessarily ensure success, that is, an efficient outcome. The successful companies, in addition to these objectives, also gave greater importance to a high level of rewards and benefits for employees,

---

* When people cannot judge a product by a 'primary' criterion (how well soap gets out dirt, that is, an outcome) then they will use a 'secondary' one (the colour of the box). Miles and Cameron (1982) found that the United States' tobacco industry has maintained productivity and profitability, both <u>outcomes</u>, but is threatened by the health and welfare <u>effects</u> of its activity, which have led to restrictive legislation and regulation controlling the industry. Industries which deal in dangerous or potentially dangerous products or practices have come under particular scrutiny in the last few decades, beginning with the environmental protest movement's agitation against insecticides. In this context, while the <u>outcomes</u> of airline deregulation have been promising, namely cheaper fares and more routes, the <u>effects</u> are threatening as consumers become more concerned about the safety of themselves and their luggage. This has been the subject of recent United States' legislation. Indeed, something that is often assumed away in the privatisation argument is that there will remain a basal level of safety, occupational health, industrial awards, and also 'corporate responsibility' over such matters as pollution, wholesome products, and so on. The most vocal opposition to privatisation, in fact, comes predictably from labour movements and less predictably but more effectively from consumer organisations.

and showed less concern for the company's prestige. Child concluded that the mix of strategic objectives influenced performance, and those firms which were more successful pursued longer term profit and growth objectives. Other factors which led to success were younger managers and better qualified managers, specifically in accounting.

Modern large scale private enterprise is also characterised by a separation of ownership and control. This so-called principle-agent relationship can raise a conflict of interests. That is, agents or managers typically have some degree of discretion to pursue non-profit maximising goals (sales, revenue, growth, quiet life) which are not consistent with the shareholders' (principal) objective of profit maximisation. The principal typically does not have enough information to detect costlessly any non-optimality in the agent's choice even if the principal (sole owner) or shareholders would wish. This creates a problem of control just as is encountered with public enterprises. The degree of managerial discretion is likely to be influenced by the conditions affecting the survival of the manager and tends to be related to the magnitude of entry costs, the cost of a 'takeover' bid and extent of market competition. For example, if a firm is very dominant and highly profitable, management's ability to operate at less than maximum technical efficiency will be enhanced. Support for this non-profit maximising behaviour of managers is provided by Domberger and Piggot (1986) who cite evidence which suggests that managerial emoluments are more closely correlated with the firm's size than profitability.

Evidence of the diminution of impact of profitability on the actions of private firms is summarised by the following quote from Kay and Thompson (1986, p. 21) ".... managers of large private firms have very little direct interest in the profitability of the organisation for which they work. Their natural concerns are with their own salaries, with the survival and growth of the firm, with its size and with the public esteem and reputation which it enjoys. All these things will be influenced by profitability, but they are distinct from profitability".

Nyman (1974) found that there was a statistically significant relationship between the absolute value of directors' shareholdings in the top 100 United Kingdom companies, and the rates of growth and profit of these companies. The higher this value, the higher was the rate of profit, but, more significantly, the higher was the rate of growth. The relationship between concentration of ownership of private sector companies, and performance is unclear. Child (1974) found that, where ownership was concentrated, chief executives attached particularly great importance to maximising profits and growth. Despite this, there were no significant links between the ownership control factor and rates of profit actually achieved.

2.2 Bankruptcy and Takeovers

Advocates of privatisation also argue that public ownership is not subject to the ultimate sanction of bankruptcy or takeover and therefore is tolerant of inefficiencies. However, for essential and powerful firms, the threat of bankruptcy or takeover of even private firms may be quite removed. For example, if a private Telecom was making losses, it is unlikely we would see government stand by and watch it fall into bankruptcy. Indeed, this has amply been demonstrated over time, the most recent example being the corporate bailout of Rothwells merchant bank in Western Australia from severe financial difficulties. In situations where governments maintain a shareholding interest in a firm, the willingness of government to allow bankruptcy to occur is even more doubtful. Similarly, private enterprise has not been reticent to ask for protection or assistance from government. A number of British nationalised firms like Leyland were not loss making because they were nationalised but, in fact, nationalised because they were loss making.

With regard to takeovers, Domberger and Piggot (p. 150) claim that the probability of takeover is inversely related to firm size. "Indeed, some companies may be so large that takeover is extremely unlikely and in this case capital market discipline would not be effective. Moreover, takeovers often have the objective of increasing or concentrating on market power which can be conducive to monopoly power and therefore allocative inefficiency". Moreover, evidence regarding the efficiency benefits achieved by takeovers and mergers is mixed.

The foregoing discussion serves in a minor way to correct the overwhelming impression gained from surveying pro-privatisation economic literature that privatisation will automatically solve the control, incentive and motivational problems which create allocative and productive inefficiencies. In short, the impact of privatisation on overall economic efficiency is not unambiguous. This, then, raises the issue of the comparative efficiency of public and private enterprises, the topic of the following section.

3. <u>The Significance of Ownership</u>

3.1 Empirical Evidence

A number of empirical studies have been undertaken to assess the comparative efficiency (that is, productive efficiency) of public and private enterprises. Transport undertakings have featured significantly in these studies. The real crux is the question: does the balance of accumulating evidence suggest privately owned operations are more efficient? Unfortunately, despite the diversity of studies, no clear picture has emerged which permits this key question to be answered with any degree of certainty.

In part, this lack of conclusive evidence stems from the inherent difficulties involved in making meaningful comparisons of the productive efficiency of alternative institutional arrangements. Ownership is only one of many factors which influences productivity. Productivity also depends, in the case of transport, on the network, capacity investment, output attributes (e.g. social objectives), physical operating environment, technology, and the competitive environment. The competitiveness of a market and its impact on efficiency warrants particular attention and is specifically addressed in the next section.

Domberger and Piggott (1986, p. 150) clearly sum up the position regarding private versus. public enterprise performance evidence:

> "Over the last 20 years a large number of studies have attempted to compare public and private enterprise performance. While this accumulation of evidence suggests certain tentative conclusions about the relative operating efficiency of private and public enterprises, there is no single study which is entirely compelling in its findings. This is because cost comparisons are rarely straightforward in the absence of a controlled experiment, and no such experiments exist for public enterprise. Among the methodological problems which arise are the difficulties in measuring capital and other costs and of standardising outputs."

The two most frequently quoted studies regarding the relative efficiencies of private and public enterprises are Borcherding, Pommerehne and Schneider (1982) and Millward (1983). Millward (1982) is often quoted in support of the relative efficiency of the public sector. Millward reviews case studies regarding electric generation and distribution in the United States, water utilities in the United States, refuse collection in a number of countries, Canadian railroads and Australian air services. He concluded that there "seems no general ground for believing management efficiency is less in a public firm" (p. 23) and finds "no broad support for private enterprise superiority" (p. 83).

Of particular interest are the studies of total factor productivity in the rail industry in Canada which has both a public operator, Canadian National (CN), and a privately owned railway, Canadian Pacific (CP). Studies by Caves and Christensen (1980) and Caves, Christensen, Swanson and Tretheway (1982) do not support the position that public enterprises operate less cost efficiently than their private counterparts. Freeman et al (1985) compared total factor productivity of CN and CP for the period 1956-1981. This analysis indicated that the absolute level of productivity for the two railways was very close and their relative positions changed a number of times. This finding is consistent with the observation that it is not the form of ownership which has the largest impact on firm productivity.

In contrast, Borcherding et al (1982), who reviewed over fifty studies in the United States and West Germany of airlines, banks, bus services, cleaning services, electricity production and weather forecasting, found only three public firms which ranked above private firms in terms of efficiency. A similarly comprehensive study of comparative efficiency in the United Kingdom has been undertaken by Pryke (1982). He analysed the performance of airlines, ferries and hovercraft, and the sale of electricity and gas appliances. Pryke concludes that "the record of the activities which I have been investigating does suggest that public ownership leads to performance which is relatively poor by private enterprise standards."

In the Australian environment, a number of studies, such as Forsyth and Hocking (1979) and Kirby and Albon (1985), have attempted to assess the relative productivity of Ansett and Australian Airlines as private and public operators in a rather unique environment. Even here, the various studies have not been unanimous in their findings. However, the weight of opinion suggests that Ansett is more efficient than Australian Airlines.

Other studies undertaken in Australia have examined the relative efficiencies of urban bus transport services as operated by public and private firms. Wallis (1979) and the Bus and Coach Association (1985) found a significant cost differential of up to 50 per cent in favour of private bus operators. Hensher (1986 and 1987) developed a method for assessing the role of ownership among the many influences on productivity. His work on factor productivity supports the notion that private supply of public transport in general has performed more efficiently than public supply by between one and nine per cent.

3.2 Comparison Difficulties

This brief review of relative efficiency studies has demonstrated the diversity of conclusions to be drawn and how difficult it is to compare public and private sector performance in any meaningful way. These studies, whilst generally supportive of the view that the private sector is more efficient, fail to conclusively provide support for efficiency gains to be achieved from privatisation. Moreover, the difficulty in isolating the impact of ownership alone on efficiency, coupled with the poor quality of data available and methods of analysis, throws further doubt on some evidence presented.

The validity of such relative efficiency comparisons is, in particular, questionable due to the distorted cost and output or service provided by public enterprises. For instance, public enterprises are frequently obliged to engage in community service obligations, support regional development and employment objectives, support domestic industry through preferential purchasing policies and redistribute income. These objectives, which may be conflicting, potentially can all adversely impact on a public enterprise cost or profit level. The existence of diverse objectives for public enterprises hinders technical efficiency comparisons and suggests technical efficiency alone is too narrow a criterion by which to judge public enterprises. Allocational objectives are inherent in a public enterprise's charter.

There are other potential reasons why the evidence is inconclusive, in particular the ambivalence of findings on the effect of structure, size, technology and organisational culture on the effectiveness of firms. The argument advanced here is that the effect of bureaucratic features on firms, public or private, is probably the chief determinant of their effectivness.

3.3 Bureaucracy

The literature on organisational theory suggests some theoretical avenues in which to search for an explanation and a major one of these is the study of bureaucracy. 'Bureaucracy' is generally used as a pejorative term indicating red tape, slowness, ineffectiveness and, by inference, public ownership. However, the modern emergence of the bureaucracy as a particular organisational type is for one very good reason, namely that it is technically superior to any other form of organisation. It is efficient, precise, speedy, unambiguous and cheap, and confers considerable power on those who wield it.

The distinction between 'public' and 'private' enterprise, epitomised by the term 'privatisation', clouds over the central fact that, organisationally, in general they are both more the same than they are different, both culturally and structurally. The modern bureaucracy, private or public, is then bound to produce a similar result, although the 'dead hand' can be manipulated to send different signals and this is the basis for the 'corporatisation' argument, as well as the on-going organisational endeavours to decentralise and produce 'skunk works' and so on in private enterprise.

Weber contrasted traditional organisational forms, namely the patrimonial and the feudal, with the bureaucratic or 'legal-rational' form which is the dominant institution of modern society.

What is meant by bureaucracy? Weber in Gerth and Mills (1948) gave the following as characteristics of bureaucracy:

- It consists of a fixed area of jurisdiction governed by rules, that is, laws or administrative regulations.

- The authority to give commands required for the discharge of these duties is distributed in a stable way and limited by rules.

- The methodical provision of the regular and continued performance of these duties is enabled by scrutiny of people's qualifications and experience.

- Entrance into an office, whether public or private, is considered an acceptance of a specific obligation of faithful management in return for a secure existence. It does not establish a loyalty to a person but to an office, community or enterprise. Contrast this with a vassal or a disciple. Officials are usually appointed, rarely elected, and anticipate a career within the organisation.

- There is a hierarchy and the levels of graded authority allow the supervision of lower offices by higher ones and the lower to appeal in a regulated manner.

- Management is based upon written documents - 'the files' which constitute 'an office', 'a bureau' or 'a department'.

- Public monies and business assets are strictly separated from the private property of the individual.

- Official business is the primary activity of the individual.

- Management of the particular office involves local rules which an individual can learn.

The modern move of some of the Commonwealth and State Public Services towards 'corporatism', namely adoption of management principles, is probably not so much a digression from bureaucratic principles as an intensification of them, a fact which has not gone unnoticed by some critics of the new system who rail at the importation of more red tape from the private sector in the name of efficiency. The sudden emergence of performance indicators and performance appraisal are examples of attempts to introduce rule and objectivity where more subjective administrative assessment formerly held sway. Other indications that bureaucracy rather than some village, feudal or other organisational form is in operation are indicated by the reaction to political appointments and/or nepotism rather than through the proper channels, and the adverse reaction to anyone found running a business on the side, while an employee of a bureaucracy, public or private.

Weber's generalisations appear to be specifically true of large firms although this, too, is controversial as is the relative influence of size versus technology. The Aston group [Pugh, et al. (1969)] attempted to determine the relative importance of a number of variables in predicting structure. These were 1) origin and history, 2) ownership and control, 3) size, 4) charter, 5) technology, 6) location and 7) dependence. A number of these variables were related to structure, specifically size, followed by technology. This was in contrast to earlier studies by Woodward (1965) which found that technology was the most influential factor in determining structure. Child (1973) concluded that larger organisations have more rules, more documentation, more extended hierarchies and are more specialised, that is, are more bureaucratic. In later work, Child (1974) found that in each of the industries studied, the more profitable and faster growing companies with 2000 or more employees were those that had developed their bureaucratic characteristics. The better performers in small firms with less than 100 employees had very little formal organisation.

3.4 Rules and Authority

Popular wisdom has it that, in private enterprise, there is an emphasis on the ready achievement of results while, in the public sector, action is put under strong safeguards to keep authority in bounds and ensure accountability. Buchanan (1975) found that middle management in four United States' business organisations was under more pressure to follow rules and authority than in the public sector. Buchanan concluded that the structural complexity and formal organisational processes of organisations in the private sector have been underemphasised.

It is assumed that the market influences organisations in positive ways, but Buchanan's study suggests that a market environment may promote stricter attendance to operating procedures and deeper personal work involvement. The latter may be beneficial, but heavy rule emphasis retards risk taking, discourages the adoption of personal responsibility and fosters rigidity in operations.

Organisational theory can also shed light on the responsiveness, or lack of it, of government organisations with respect to private organisations. Porter and Van Manaan (1970) examined time management of managers from city governments versus industrial organisations. The city governments elected were expected to conform to the council-manager plan, namely that they should run as much like a 'business' as possible. Hence, they were, to some extent, 'matched' with the business group by an emphasis on 'efficient operations'. Porter and Van Manaan found that government managers needed to respond to far more external-to-the-organisation demands, and placed more weight on the views, needs, and demands of outsiders than they did on their individual views. They felt that they had much less time control than the private managers because of intrusions from the outside world and spent 17 per cent of their time on the telephone, and 18 per cent on their own. By contrast, private managers spent 9 per cent on the telephone and 25 per cent of their time on their own. These results were supported by other research, suggesting that government managers receive far more communication from outside the organisation.

3.5 Is Ownership Significant?

This section has been concerned with the issue of the significance of ownership on outcomes of the organisation. However, the possibility and merit of dividing organisations into two homogenous groups, private and public, is doubtful. For each major dimension of an organisation, specific entities can be located on a spectrum. The field of business and size is probably as much a differentiating factor as whether the ownership is public or private. There is probably as much difference between CRA, or Pierre Cardin Inc., and a family firm as there is between those companies and a State bank or rail authority.

Are public and private management inherently different? Again, there is no consensus on whether they are or are not and, if so, in what respects. Contrasting views in the long running debate can be found in Perry and Kraemer (1983). These observations, coupled with a lack of empirical evidence to support the superiority of private ownership, suggest that ownership itself is not as significant an issue as the current debate suggests.

4. <u>Other Issues</u>

4.1 Competition and Efficiency

Although there may be a diversity of viewpoints regarding the relationship between ownership and efficiency, the position in the economics literature regarding competition and efficiency is far more clear cut. There is general agreement that the efficiency of both private and public firms is enhanced within a competitive environment.

Borcherding et al (1982), for instance, concludes that "it is not so much the difference in the transferability of ownership but the lack of competition which leads to the often observed less efficient production in public firms" (p. 136).

Similarly, Kay and Thompson state that "no simple generalisation about superiority of private sector performance can be sustained. But there is support for the view that the efficiency of all firms, public or private - is improved by a competitive environment" (p. 25).

Furthermore, they state "It follows that privatisation into an uncompetitive environment is likely to be positively harmful ....".

This raises concern about the interaction between privatisation and deregulation and possible conflict. While the price obtained for a public enterprise will be maximised by retaining regulatory barriers to entry or even regulating to maintain monopoly status, the longer term efficiency gains to be achieved through competition may be attenuated. The Thatcher Government's motivation with regard to competition may be questioned.* When the Tories came to power in Britain in 1979, they said that the true reason for privatisation was to introduce competition for the benefit of the consumer. The monopoly was viewed with suspicion. However, in a recent policy statement, the government asserted that it plans to privatise natural monopolies where competition "does not make business or economic sense" [see Kay and Thompson (1968)]. British Telecom and British Airways have been privatised in toto.

Heald (1985) goes even further regarding the possible conflict between ownership and deregulation and states in relation to the United Kingdom - particularly British Telecom - "If a radical government cannot secure such changes [liberalisation] before denationalisation, the subsequent chances must be bleak because the private shareholder will then be able to claim that there are questions of trust and credibility at stake. Decisions are now being taken which close future options in the sense that, if not literally irreversible, the financial and political costs would be formidable deterrents" (p. 9).

It would appear from the economic literature, then, that perceived benefits to be achieved from competitive policies exceed those to be gained from change in ownership. This is at odds with public discussion on privatisation and stems in part from a lack of understanding that the competitive and ownership policies are distinct.

4.2 Control and Incentives

The following three sections briefly raise a number of issues which are further afield yet warrant consideration in a wider perspective of privatisation. Further development of these ideas in the debate on privatisation would appear to be called for.

Privatisation can be seen as a reaction to disenchantment with the performance of public enterprises stemming from the control and incentive problems associated with public ownership. Littlechild (1983), for example, contends that "privatisation represents a significant change of approach: an acknowledgement that many of the problems of nationalised industries are inherent in nationalisation

---

* The Thatcher Government's hidden agendas in privatisation include wider public share ownership, weakening unions, and other public policy issues. These are also controversial and would go too far afield in this paper. However, one issue in particular deserves closer scrutiny and is apt to be overlooked in the context of transport. That is the matter of technology and this is particularly evident in telecommunications and is briefly discussed in the Appendix.

itself, and that progress can only be made by structural changes - that is, by introducing competition and private capital" (p. 19). The failure of successive economic and financial controls contained within a series of British White Papers and committees to increase the efficiency of public enterprises is seen as evidence of the inherent problem of controlling such enterprises. This point of view is summarised by Heald (1985) "the failure of successive control systems is interpreted as evidence, not of defective design and implementation, but of some deeper insolubility which cannot be remedied just by devising new systems of control because public enterprise is viewed as a flawed instrument of public policy" (p. 8).

However, the need to confront control and incentive issues remains under private ownership, particularly when there are monopolies involved or subsidies required. This is illustrated by the action taken by the British Government to set up OFTEL (the Office of Telecommunications) to regulate British Telecom following its sale and then OFGAS to regulate the British Gas Corporation. Natural monopolies raise policy problems whether they are in public or private hands. For example, in the United States, Averch and Johnson (1962) noted, among privately owned public utilities subject to rate-of-return regulation, inefficient factor use and excessive capital investment to extend their capital rate base. Moreover, the possibility of regulatory capture, whereby the regulating body becomes the captive of the industry itself rather than acting in the interests of the public, is not removed by private ownership of the enterprise.

4.3 Equality of Service Provision

Successive governments have deemed it to be in the public interest for Australians to have access to comparable basic services at an equitable cost regardless of where they live. Any serious discussion of privatisation must take account of the 'no slum States' argument which has prevailed since Federation and has guided the deliberations of the Commonwealth Grants Commission. Social service obligations such as services to isolated communities or prices set below cost to particular groups can continue to be met under private ownership through alternative means - like direct subsidy to the provider. Whilst this is entirely feasible, we note that there is some concern regarding the effect of subsidies on cost levels of both private and public operations. This calls into question the gains to be achieved by privatising and then subsidising specific activities.

4.4 Public Interest

Walsh (1978, p. 334), in an analysis of the success of the many public corporations in the United States, draws attention to a persistent flaw in the American arguments.

> "American government and society have failed to develop a consensus on the values and patterns of behaviour appropriate for those who participate in public institutions. Americans do not believe in the public interest. When government corporations (or other agencies, for that matter) assume the aspect of runaway horses, the cause is more often the absence of any rider in the saddle at all than the superior strength of a determined beast."

She adds that the United States has a fear of collective action. Britains, too, value the individual above the community and private interests above public [see Marquand (1988)]. It is possible that privatisation is another cultural import, a successor to the enchantment with Japanese management techniques just a few short years ago which were also claimed to increase productivity. However, without acknowledging specificity of environments and the particularity of the situation, it is unlikely that local talents will be tapped. Wettenhall (1987) has hinted at the Australian pragmatism, and we would like to think that this stems from at least an acknowledgement of public interest, if not a fostering of it. This would tend to indicate a somewhat different starting point for policy development.

5. Conclusion

The economic argument for privatisation provides, at best, mixed conclusions as to its efficacy. These conclusions are not bolstered by other arguments from the organisational literature. As a consequence, we contend that the efficiency and effectiveness with which organisations carry out their business is a significantly more complex issue that is encompassed by a distinction between private and public ownership, a factor which, in particular, is glossed over in the economics literature. In addition, scrutiny of actual British privatisation outcomes leads to the inference that what has occurred was not primarily motivated by considerations of efficiency and it is tempting to say that efficiency concerns were only of secondary importance in the issue of privatisation. Since consideration as to what actually did motivate British privatisation remains largely speculative, it becomes almost impossible to judge whether privatisation has been an appropriate method of achieving its intended objectives.

If, then, privatisation seems like a non-topic, it is perhaps for two reasons. The first is that it is embedded in an intransigent historical argument over the best way to run society. The second is that any consistent empirical proof has not been forthcoming from the research community. As a consequence, the only feasible course of action would be for privatisers to consider carefully the merits and disadvantages of each particular case, rather than subscribing to the theory of the universal fix.

APPENDIX

PRIVATISING BRITISH TELECOM

It is, perhaps, misleading to argue from the transport perspective alone as, for the most part, it has a specific technical characteristic, namely, it is modular. By contrast, telecommunications rely particularly on access into both a vertical and horizontal network. The large telecommunications companies are aiming at end-to-end transmission of information in the global market. For this reason, IBM has diversified into transmission and information provision, AT&T into data processing, and information providers, e.g. Reuters, airlines, and banking, into transmission. GM, a large user of communications services, is also moving into information technology.

IBM has 70 per cent of the installed data processing capacity in Europe and is looking to break into transmission. AT&T, which dominates transmission, is looking to data processing and has a 25 per cent stake in Olivetti and a joint venture with Philips. Much European policy is seen as a move to prevent further domination by IBM. For example, France has rationalised its electronics sector in order to create companies of a size which can compete with the American companies. Hills (1986, p. 186) states that "one of the original intentions of the government in privatising British Telecom - to create a company capable of competing against the American giants - has been followed by government instigation of a merger between the two manufacturers, GEC and Plessey."

In her review of 'Telecoms' in the United States, Britain and Japan, Hills concluded that the current round of privatisation and liberalisation has resulted in each country in the emergence of one overwhelmingly dominant private entity which remains regulated. In the case of British Telecom (BT), the hidden agenda appears to be technology driven, namely the shift in the communications market from three distinct segments, long-lines, equipment and local networks, to one, namely end-to-end transmission of information in the international market. By emulating the United States telecommunications industry, BT perhaps hopes to gain an edge in the high technology service sector of the communications revolution.

REFERENCES

Abelson, P.W. (ed.) (1986) Privatisation, The Australian Experience, Australian Professional Publishers, Sydney.

Abelson, P.W. (1986) Privatisation: A Point of View, in Privatisation, The Australian Experience, edited by Abelson, P.W., Australian Professional Publishers, Sydney.

Albon, R (1986) The Scope of Privatisation in Australia, CEDA Melbourne.

Averch, H and Johnson, L.L. (1962) Behaviour of the Firm Under Regulatory Constraint, American Economic Review, Dec. p.1052-1069.

Beesley, M and Littlechild, S (1983) Privatisation: Principles, Problems and Priorities, Lloyds Bank Review, July 1-20.

Bly, P.H., Webster, F.V. and Pounds, S. (1980) The Effects of Subsidies on Urban Public Transport, Transportation 9

Borcheiding, T.E., Pommerehne, W.W. and Schneider, F. (1982) Comparing the Efficiency of Private and Public Production: The Evidence from Five Countries, in Bos, D., Musgrave, R.A. and Wiseman, J. (ed.), Public Production.

Buchanan II, B. (1975) Red Tape and the Service Ethic: Some Unexpected Differences Between Public and Private Managers, Administration and Society, Feb. p.423-444.

Bus and Coach Association, NSW (1985) The $90m Case for Private Buses, Sydney.

Button, K.J. (1984) Subsidies and the Provision of Urban Public Transport, International Journal of Transport Economics, Aug-Dec Vol. XI, No 2-3.

Cacioppe, R. and Mock, P. (1987) A Comparison of the Quality of Work Experience in Government and Private Organisations, Human Relations 37:11 p 923-940

Cameron, K.S. (1986) Effectiveness as Paradox: Consensus and Conflict in Conceptions of Organisational Effectiveness, Management Science, Vol. 32 No. 5, May p.539-553.

Caves, D.W., Christensen, L.R., Swenson, J.A. and Trethaway (1982) Economic Performance of US and Canadian Railroads: The Significance of Ownership and the Regulatory Environment, in Managing Public Enterprise, ed. by Stanbury, W.T. and Thompson, F.

Caves, D.W. and Christensen, L. (1980) The Relative Efficiency of Public and Private Firms in a Competitive Environment: The Case of Canadian Railroads, Journal of Political Economy, p 958-76.

Cervero, R. (1983) Cost and Performance Effects of Transit Operating Subsidies in the United States. International Journal of Transport Economics, Dec. Vol. X, No. 3.

Child, J. (1973) Predicting and Understanding Organisation Structure, Administrative Science Quarterly 18 (June) p. 168-185.

Child, J. (1974) What Determines Organisational Performance, Organisational Dynamics, 3:(1) p.2-18.

Chin, O. & Webb, G (1986) Privatisation: A View from the Private Sector, in Privatisation, The Australian Experience, edited by Abelson, P.W., Australian Professional Publishers, Sydney.

Clarke, R. and Porter, M. (1982) State Enterprise Accountability: A Contradiction in Terms. Centre of Policy Studies, Monash University.

Consumer Interest (1987), September.

Cransten, R. (1986) Privatisation: A Critique, in Privatisation, The Australian Experience, edited by Abelson, P.W., Australian Professional Publishers, Sydney.

Cyert, R.M. and March, J G (1963) A Behavioural Theory of the Firm, Englewood Cliffs, N.J.: Prentice Hall.

Domberger, S. and Piggott, J. (1986) Privatisation Policies and Public Enterprise: A Survey. The Economic Record, June p 145-162.

Freeman, K.D., Oum, T H., Tretheway, M W. and Waters, W.C. (1985) The Total Factor Productivity of the Canadian Class 1 Railways 1956-1981 Logistics and Transportation Review 21 (3).

Gerth, H.H. and Mills, W.C. (1948) From Max Weber, London, Routledge and Kegan Paul.

Haritos, Z.J. (1985) CN and Public Policy: Review of Issues, University of Toronto/York University, Report No. 1986/04.

Heald, D. (1985) Will the Privatisation of Public Enterprises Solve the Problem of Control? Public Administration 63(1) p.7-22.

Hensher, D. (1986) Productive Efficiency, Ownership and Contracting Out of Transport Services, in Privatisation, The Australian Experience, edited by Abelson, P.W., Australian Professional Publishers, Sydney.

Hensher, D. (1987) Productive Efficiency and Ownership of Urban Bus Services, forthcoming Transportation.

Hensher, D.A. (1987) Productivity in Privately Owned and Operated Bus Firms in Australia, memo.

Hills, J. (1986) Deregulating Telecoms: Competition and Control in the United States, Japan and Britain, Frances Punter (Publishers) London.

Independent Inquiry into Domestic Airfares (1981) Volumes I-III (The Holcroft Inquiry), AGPS.

Independent Review of Economic Regulation of Domestic Aviation (1986) (The May Inquiry) AGPS.

Kay, T., Mayer, C. and Thompson, D. (1986) Privatisation and Regulation, The UK Experience, Clarendon Press, Oxford.

Kay, J. and Silbersten, S. (1984) The New Industrial Policy — Privatisation and Competition, Midland Bank Review, Spring p. 8-16.

Kay, J. and Thompson, D. (1986) Privatisation: A Policy in Search of a Rationale, Economic Journal, 18-32.

Kirby, M.G. (1981) Domestic Airline Regulation: The Australian Debate, Research Studies in Government Regulation, 1, Centre for Independent Studies, Sydney.

Kirby, M.G. and Albon, R.P. (1985) Property Rights, Regulation and Efficiency: A Further Comment on Australia's Two Airline Policy, Economic Record, 61 June p 535-539.

Littlechild, S.C. (1983) Problems of Controlling State Enterprises, in State Enterprise and Deregulation, Centre of Policy Studies, Monash University.

Marquand, D. (1986) The Unprincipled Society: New Demands and Old Politics, Jonathan Cape.

Mansfield, B. (1986) The Public Sector: Efficiency and Equity, in Privatisation, The Australian Experience, edited by Abelson, P.W., Australian Professional Publishers, Sydney.

March, J.G. and Simon, H.A. (1958) Organisations, New York: John Wiley

Millward, R. (1982) The Comparative Performance of Public and Private Ownership, in Lord Roll (ed.) The Mixed Economy, Macmillan, London

Nyman, S. (1974) quoted in Nyman, S and Silbersten, A. (1978) Ownership and Control of Industry, Oxford Economic Papers 30(1) p. 74-101.

Officer, R.R. (1983) Accountability and Monitoring the Performance of the State Enterprise, in State Enterprise and Deregulation, Centre of Policy Studies, Monash University.

Perry, J.L. and Kraemer, K.L. (1983) Public Management: Public and Private Perspectives, University of California, Mayfield Publishing Coy p. 55-108.

Peters, T.J. and Waterman, H. (1982) In Search of Excellence, New York, Harper Row.

Piggott, J. (1986) Privatisation and Public Economics — Some Neglected Issues, in Privatisation, An Australian Perspective, edited by Abelson, P.W.

Pincus, J.J. (1983) Regulation and Public Enterprise, in State Enterprise and Deregulation, Centre of Policy Studies, Monash University.

Policy Guidelines for Commonwealth Statutory Authorities and Government Business Enterprises (1987), AGPS Canberra.

Porter, M. (1986) The Burden of Government Regulation and Public Ownership, Centre of Policy Studies.

Posner, M. (1984) Privatisation: The Frontier Between Public and Private, Policy Studies 5(1) p.22-32.

Pryke, R. (1982) The Comparative Performance of Public and Private Enterprise, Fiscal Studies 3(2) p.68-81.

Pucher, J. and Markstedt, A. (1983) Consequences of Public Ownership and Subsidies for Mass Transport: Evidence from Case Studies and Regression Analysis, Transportation II.

Pucher, J., Markstedt, A. and Hirshman, I. (1983) Impacts of Subsidies on the Costs of Urban Public Transport, Journal of Transport Economics and Policy.

Pugh, D.S., Hickson, D.J., Hinings, G.R. and Turner, C. (1969) The Context of Organization Structures, Administrative Science Quarterly (14) p. 91-114

Shackleton, J. (1984) Privatisation: The Case Examined. National Westminster Bank Quarterly Review, May

Simon, H (1957) Models of Man, New York, John Wiley

Statutory Authorities and Government Business Enterprises (1986) A Policy Discussion Paper, AGPS.

Trengrove, C. (1986) Privatisation — A Relevant Word for Australia? Centre of Policy Studies

United Kingdom (1967) White Paper: Nationalised Industries: A Review of Economic and Financial Objectives, Cmnd 3437, HMSO London.

United Kingdom, (1978) White Paper: The Nationalised Industries, Cmnd 7131, HMSO London.

Wallis, I. (1979) Private Bus Operations in Urban Areas — Their Economics and Role, Fifth Australian Transport Research Forum.

Wiltshire, K. (1986) Privatisation, The British Experience, An Australian Perspective, CEDA Study.

Walsh, A.H. (1978) The Public's Business. The Politics and Practices of Government Corporations, MIT Press.

Wettenhall, R. (1987) Public Enterprise and National Development, Royal Australian Institute of Public Administration, Canberra.

Woodward, J. (1965) Industrial Organisation Theory and Practice, London, Oxford University Press.