

## **Privatization: A Multi-Theory Perspective**

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*For decades, privatization has become one of the most important elements of the structural reform agenda in developed and developing countries. From a management perspective, this study makes an attempt to provide theoretical insights into two interrelated questions: (a) why does a country decide to undergo privatization in some industries but not others; and (b) why do some countries enjoy success while others experience failures from privatization? This study developed propositions through the lens of seven organizational theories. From multiple theoretical perspectives, this study offers research implications as well as practical implications to practitioners and policy makers.*

### **INTRODUCTION**

For several decades, privatization has become one of the most important elements of structural reform programs in both developed and developing countries (Sheshinski & Lpez-Calva, 1999). According to Megginson and Netter (2001), the political and economic policy of privatization is broadly defined as the deliberate sale by a government of assets or state-owned-enterprises (SOEs) to private economic agents. Since its introduction by Britain's Thatcher government in the early 1980s, privatization has been widely in use in more than 100 countries (Megginson & Netter, 2001), and has had a remarkable impact on the society as a whole (Prizzia, 2005; Xu & Lee, 2012).

Theoretically and economically, privatization helps establish a free market and foster competitions which, in turn, give the public greater choices at a competitive price. Based on efficiency considerations, D'Souza and Megginson (1999) argued that, not only the customers of privatized enterprises enjoy benefits from privatization, but also, as the enterprises become more efficient, the whole economy will benefit. The economic prosperity gives government a means to maximize social welfare which furthers its legitimacy. For example, Boles de Boer and Evans (1996) examined the impact of the 1987 deregulation and 1990 privatization of Telecom New Zealand on the price and quality of telephone services. They found significant declines in price of phone services, significant improvement in service quality, and significant benefit to its shareholders. Similarly, in the airline industry facing competitions globally, Eckel, Eckel, and Singal (1997) analyzed the effect of privatization on the performance of British Airways, and documented increased competitiveness of the privatized organization in comparison to its closer rivals (i.e., its U.S. competitors). Ideally, as Megginson and Netter (2001) stressed, privatization propels a country to establish an integrated political, social, and economic system that boosts income and welfare for all citizens.

However, privatization "is almost never painless" (Kikeri & Nellis, 2002, p. 20), and, worse, may result in spectacular failures in some cases (Li, Wang, Cheung, & Jiang, 2011). Because privatization involves changing institutional archetypes which structure the governmental, societal, and economic

arrangements and behaviors, it can be both challenging and problematic (Greenwood & Hinings, 1993; Li et al., 2011). Privatization may result in a decline in national economy, as demonstrated by a study of mass privatization in 25 post-communist countries (Hamm, King, & Stuckler, 2012). It can also potentially cause tremendous social upheaval in the short term, since privatization is often accompanied by large numbers of redundant workers (Megginson & Netter, 2001). In Poland, for instance, the unemployment rate increased by 8 percent between 1990 and 1996 during which the country underwent privatization (Sheshinski & Lopez-Calva, 1999). Moreover, privatization can potentially trigger political instability, especially when inequality in distributions of income and wealth increases significantly (Stiglitz, 2002). For example, the former Soviet reformers suddenly abolished the former centrally planned institutional framework that had held the society and economy together through an “iron fist” for over 70 years, and launched a mass privatization in 1992 (Tan, Li, & Xia, 2007). Its goal was to make all citizens owners of private property as quickly as possible with the least amount of social conflicts (Kim & Yelkina, 2003). However, the good intention did not produce good outcomes: Russia's gross domestic product (GDP) declined 41 percent between 1992 and 1995, unemployment rose from almost zero at the end of 1991 to approximately 7 percent by October 1995, living standards declined, inequality grew dramatically, and citizens' incomes fell, resulting in the electoral success of a resurgent of Communist Party in 1996 (Gerber & Hout, 1998). In essence, privatization is such a complex phenomenon that it is intertwined with multiple factors such as economic considerations, social sensitivities, and political concerns. As such, making privatization policy decisions and using state interventions to manage privatization programs in balancing these multiple factors have been critical issues to the success or failure of privatization.

Although the literature on privatization has grown, much attention is still required to enhance the extant body of knowledge theoretically and practically (Ramamurti, 2000). There is a dearth of research on privatization, specifically in the management literature (Zahra, Ireland, Gutierrez, & Hitt, 2000). One of the reasons for this gap may be the fact that management research typically focuses on individual-, group-, and/or organizational-level, while privatization research focuses on industry and/or country level (Kim & Yelkina, 2003; Ratto-Nielsen, 2004; Wright, Hoskisson, Filatotchev, & Buck, 1998). Another reason may be that management research often is not carried out in a systematic way, thus unable to adequately address a phenomenon (Frost, 1980). In this study, from a management perspective I attempt to look into privatization at the nation-level through the lens of well-established organizational theories. Specifically, by applying organizational theories to privatization, this study addresses two interrelated questions: (a) why does a country decide to undergo privatization in some industries but not others; and (b) why do some countries enjoy success while others experience failures from privatization? The assumptions of this study are: (a) governments represent public interests; and (b) privatization decisions are based on governments' intentions to improve economic efficiency and societal welfare.

This study makes several contributions. First, this study views privatization systematically from a management perspective. Second, this study takes a balanced view by looking into both economic and social performance of privatization. Studies on the effectiveness of privatization tend to emphasize economic outcomes such as cost reductions, profit, and revenue (Prizzia, 2001; Stolt, Blomqvist, & Winblad, 2011). Recently, some researchers argued that privatization outcomes should include both economic and social performance, because together they measure whether a country achieves long-term broad-based sustainable development through its privatization program (Hodge, 2000; Parker & Kirkpatrick, 2005; Prizzia, 2001). Third, by applying multiple theories to privatization, this study aims at enhancing our understanding of privatization as well as providing a broad foundation for future research on privatization. Fourth, from multiple theoretical perspectives, research and practical implications of privatization are offered.

## **THEORETICAL PERSPECTIVES APPLIED TO PRIVATIZATION**

In this study, privatization is viewed through the lens of seven organizational theories, namely, systems theory, contingency theory, real options theory, institutional theory, agency theory, resource

based views, and transaction cost economics. Specifically, these organizational theories were applied to privatization and theoretical propositions were developed. Table 1 summarizes the key premise of each theory, and the respective key insights for privatization and propositions. (See Appendix for Table 1)

### **Systems Theory**

Systems theory suggests that a system can be classified according to its common property and is consist of interrelated entities of activities (Ashmos & Huber, 1987; Scott, 2003). The system defines and redefines itself among its internal components as well as its relationship with the external environment, aiming at correcting errors in the direction of increasing compatibility between the system and the environment (DiMaggio & Powell, 1983). In this regard, a country can be viewed as an integrated political, social, and economic system that interacts with the world (i.e., the environment). The country's system is composed of interrelated entities such as government agencies, private and public organizations, and the general public. If the system is disassembled in any way (e.g., one or some SOEs in the system are privatized), the properties of both the components (i.e., the SOEs) and the system as a whole are changed consequently (Ashmos & Huber, 1987). So is its relationship with the environment.

From such a perspective, a country's system is an open system that is affected by both external (i.e., global competitions, scientific breakthroughs, demands for resources) and internal (i.e., domestic economic failures, unemployment rate, political legitimacy) factors. A country's system imports energy (e.g., privatization programs and knowledge, global competitiveness) from its external environment (e.g., foreign countries) (Katz & Kahn, 1966). These external factors impact whether and how the country undergoes privatization. In reality, nowadays, in an increasing competitive global environment, a country may be forced to respond to external pressures through its purposeful ownership change of privatization, aiming to maximize its economic efficiency and social responsibility as well as competitiveness in the global market. For instance, China is one of the few countries where privatization and globalization efforts have been carried out at the same time since the country adopted a policy of opening-up and reform in 1980. Today, the private economy plays an important role in China's economy. In Shenzhen, China's fourth largest economy, for example, the private sector generated over 50 percent of the fiscal revenue of the city (Shenzhen Government Online, 2007).

*Proposition 1a. The stronger global competitions countries face, the more likely a country will undergo privatization.*

Internally, on the other hand, a country's system utilizes the energy (e.g., other countries' privatization programs and knowledge) and corrects errors (e.g., market failures) through implementing its own privatization program, thus increasing compatibility between the system and its environment (Katz & Kahn, 1966). In response to disappointing SOE performance and in an attempt to create substantial and enduring benefits to its economy and citizens in a competitive global market, governments seek ways to correct market failures (e.g., low efficiency, financial constraints), one of which notably is privatization. The larger the failure, the wider spread-out the privatization. In China, for instance, 72 percent of SOEs were not profitable in 1995 (Kikeri & Nellis, 2002). Since China launching its privatization program, the number of SOEs fell by 40 percent between 1996 and 2001 and many remaining SOEs were scheduled for privatization (Garnaut, Song, Tenev, & Yao, 2003). Today, China is the world's second-largest economy with the most dynamic GDP growth. The success in China may be due to the fact that, similar to New Zealand, the U.K., Mexico, and Chile, privatization was accompanied by reforms to open markets, remove price controls, and encourage the development of the private sector through free entry (World Bank, 1992).

*Proposition 1b. The less efficient SOEs are, the more likely a country will undergo privatization.*

When one or more SOEs in the system are being privatized, the property of the country's system is changed consequently (Scott, 2003). Such a change has an effect on all interconnected components (i.e., private and public organizations, government, the public) in the system, since these components that are open to, and interact with, the system. However, the strength of this effect is primarily determined by the scope of privatization and the nature of interdependent relationships between the privatized organizations and their interconnected components in the system. As the scope of privatization, the ambidextrous relationships between the privatized firms and their interconnected components, the uniqueness of the assets owned by the privatized firms, and the importance of products or services by the privatized firms to the general public increase, the complexity of privatization and its impact on the functionality of the entire system increase. As a result, government may choose not to privatize certain industries that are important to a country's economy and social welfare, but begin privatizing non-essential SOEs at a small scope. For example, a country may not privatize essential services such as water, electricity, and health care, especially at its early stage of privatization (e.g., Joseph, 2010; Manuel, 2003; Stolt et al., 2011). Even, in some cases, when these essential services are privatized, tight regulations and close monitoring programs are in place, because privatization is a complex phenomenon that is interwoven and intertwined with economic considerations, social sensitivities, and political concerns.

*Proposition 1c. The more important industries are to a country's economy and social welfare, the less likely these industries will be privatized in early stages of privatization.*

From a dynamic systems perspective, privatization is not a one-shot event but a process that can occur in stages (Ramamurti, 2000), because no country wants to bet its economy on a rapid, irreversible privatization program without some assurance that all necessary prerequisite policies have been put in place (Megginson & Netter, 2001; e.g., Kim & Yelkina, 2003). This suggests that, in order to achieve economic prosperity in a socially responsible way, it is essential for a country to manage its privatization process through feedforward, concurrent, and feedback control mechanisms. Because privatization programs affect a country's political, economic, and social components, information from these control mechanisms provides insights for a country to proactively manage and improve its privatization policy and process in order to achieve desired outcomes (Ratto-Neilsen, 2004). For instance, information from previous rounds of privatization can influence the content and context in which the subsequent rounds of privatization are designed and implemented. In practice, government may begin its privatization program by selling small and non-essential SOEs in one sector, allowing limited new entry into the sector, and creating a new law or regulatory agency for the sector (Hamm et al., 2012; Parker & Kirkpatrick, 2005). This, if successful, may be followed by full privatization of ownership, further deregulation, and measures to make regulation more effective in the sector and beyond (Ramamurti, 2000). Or, this, if unsuccessful, may lead to other privatization alternatives (e.g., partial privatization of ownership) or even nationalization. Therefore, sequencing and staging of privatization are critical issues and control mechanisms must be in place (Megginson & Netter, 2001).

*Proposition 1d. The better sequencing and staging of privatization are managed, the more successful privatization will be.*

### **Contingency Theory**

Contingency theory contends that policy makers must interpret the environment correctly and maintain fit through changes (Child, 1972). In the case of privatization, a country's internal (i.e., culture, social norms, resources) and external (i.e., global competitions; geo-political coalitions) environmental conditions are posited as critical constraints upon the choice of privatization. Privatization policy makers must examine the environment and understand the holistic nature of the changing environment impacted by these conditions. As mentioned in the systems theory section, these environmental factors place great demands on a country's entire system in general and on economic, social, and political subsystems specifically. As such, privatization decisions should be contingent upon these environmental factors

(Lawrence & Lorsch, 1967). Further, the fit between a country's system and the environment can be increased, if the system is open to continual redefinitions (i.e., a planned market, a free market, or a mixed market) and corrections (i.e., market failures, financial constraints; Lawrence & Lorsch, 1967).

However, there is no one best way to privatize (Lawrence & Lorsch, 1967). Every country has its own unique environment that historically constitutes a set of forces (e.g., law, culture and norms) to be adapted to, co-aligned with, controlled, or controlled by (Smircich & Stubbart, 1985). Privatization decisions, based on efficiency grounds and justified on welfare grounds (Brada & Ma, 2007), should reflect the norms of the social, cultural and political domination (Davis, 1982). For instance, a World Bank (1996) study concluded that, the inclusion of social factors (i.e., welfare, social services, and equity) and the participation by all stakeholders in the privatization process is far more important in the European transition economies and developing economies than in developed countries. Therefore, from a contingency theory perspective, the uniqueness of a country's environment requires privatization policy makers to take full considerations economically, politically, and socially, and adopt experimentations contingent upon the environment.

Taken together, the effectiveness of privatization may depend upon the following proper fits: (a) between a privatization program and a country's (internal and external) environment; (b) between subsystems (i.e., public and private sectors, government, the public) and a country's environment; and 3) among subsystems within the system. The first two fits can be viewed as differentiation and the last as integration (Lawrence & Lorsch, 1967). Moreover, government needs to make strong political commitment to lead its privatization programs and to effectively resolve conflicts arising from the programs (Lawrence & Lorsch, 1967). When a privatization program is contingent upon a country's environment, the success of the program economically, socially, and politically is high.

*Proposition 2. Countries developing their privatization programs contingent upon the country's environment are more likely to succeed than those who do not.*

### **Real Options Theory**

Real options theory has emerged as a compelling approach for evaluating investment opportunities in uncertain environments (Leiblein, 2003). According to this theory, a real option is the right, but not the obligation, to undertake privatization in an uncertain environment, so that privatization programs can create economic and social values through operating flexibility (Leiblein, 2003).

Historical experience and knowledge may be viewed as carriers of wisdom (March & Olsen, 1984). If a country has no prior experience or knowledge of privatization, uncertainty and unpredictability of privatization outcomes tend to be heightened. By choice or by chance, a country may view other countries' successful privatization programs as options and simply adopt an available program. However, a country should not completely obligate itself to the similar program but instead, reserve its rights to evaluate and modify the programs, because every country operates under a different environment which bears its own social, cultural, and political identity. For example, within developing and emerging economies, as opposed to developed economies, the economic and social importance of SOEs is far greater, the environment is less market-friendly, less elastic, and more uncertain, the private sectors are well underdeveloped, and the government capacity to regulate a competitive market tend to be poorer (Parker & Kirkpatrick, 2005).

According to Ramamurti (2000), privatization can be *broad* (i.e., sale of public assets and deregulation of an entire industry) or *narrow* (i.e., transfer of partial ownership or control of a sector to private enterprises). Narrow form of privatization can be viewed as a real option in an uncertain environment, because it provides government great flexibility when operationalizing privatization. Government can choose to increase the scope of privatization if early rounds of privatization are successful, or, regulate the sector or even take over the privatized firms if early rounds of privatization are unsuccessful. For example, India partially privatized its electricity industry by introducing a parallel market (i.e., market-based production sector and state-run sector) in the country (Joseph, 2010). Moreover, due to the essential nature of electricity services to its economy and citizens' everyday life, the

government chose to keep the industry regulated and maintain the right to nationalize the privatized sector in the event of non-improvement in efficiency and poor services by the privatized enterprises. The uncertain environment, coupled with the unique country identity, requires policy makers to evaluate possibly privatization programs, customized its own program with a wide range of options (e.g., privatization, liberalization, and different combinations), and manage it with flexibility.

*Proposition 3. In uncertain environments, countries, who undergo privatization with a wide range of options and manage it with flexibility, are more likely to succeed than those with a single, rigid privatization option.*

### **Institutional Theory**

Neo-institutional theory portrays large institutional structures (e.g., organizations, government agencies, countries) as rationally coherent autonomous actors whose behaviors are guided by social structures such as law, culture, and norms (March & Olsen, 1984). The actors, on the one hand, coherently institutionalize and legitimize decisions (e.g., privatization programs) to conform to their environment (e.g., social norms and competitive pressures). On the other hand, they autonomously develop and shape the public's understanding of the decisions and alternatives (e.g., new regulatory agencies). In the privatization case, government policy makers, guided by the social structures, correct market failures through institutionalizing and legitimizing privatization programs that appropriately reflect the country's history and culture (Scott, 1995). For example, Chinese government has systematically introduced certain capitalist market-based enterprises to liberalize the market and correct market failures, while attempted to preserve the socialist institutions in order to maintain its legitimacy and protect their power base (Tan et al., 2007). Success after implementation of the first round of privatization more likely leads to embracing the program in subsequent rounds, whereas failure may lead to other alternatives (e.g., partial privatization and regulations) and even an opposite direction (e.g., nationalization). Therefore, an effective and efficient institutional system is critical to the success of privatization. For instance, in the sale of Chile Telecom, the consumers, labor, government, and buyers all benefited and the productive efficiency of the company increased as a result of a well-developed, well-administered regulatory framework (World Bank, 1992).

*Proposition 4a. Countries who pursue privatization and institutionalization simultaneously are more likely to succeed than those who pursue one without the other.*

Another avenue of institution theory deals with isomorphism. DiMaggio and Powell (1983) argued that highly structured institutions (e.g., government agencies, SOEs) provide a context in which individuals' efforts to deal with uncertainty and constraint often lead to homogeneity in institutions' structure, culture, and output. This implies that, in the privatization case, uncertainty may be a driving force that encourages a country simply to imitate other countries' successful privatization programs which are available and accessible. Mimetic isomorphism is the result of a country reacting to its unknown and uncertain environment by modeling itself after successful privatization programs in other countries (DiMaggio & Powell, 1983). Throughout the privatization history, many emerging economies launched ambitious programs to privatize their SOEs with the intention of replicating the success of privatization programs in developed economies (Megginson, Nash, & Van Randenborgh, 1994). However, such efforts did not always produce expected outcomes as what were in the developed economies. Examples of failing to achieve efficiency and social responsibility can be found from the privatization in Russia (Wright et al., 1998) and in Poland (McDonald, 1993). As such, simply imitating other countries' successful privatization programs may not be an optimal solution to a country's privatization.

*Proposition 4b. The more uncertain a countries' environment is, the more likely the country will imitate other countries' successful privatization programs.*

## **Agency Theory**

Agency theory is concerned with managing principal-agent relationships (Eisenhardt, 1989). Based on this theory, in the privatization case, a government is the principal, and privatized enterprises are the agents. Government, representing public interests, has goals of maximizing social welfare, fostering its economy, and maintaining high level of employment. Privatized organizations have their own objectives mainly focusing on maximizing profit and shareholder-wealth. Principal-agent problems arise when government and privatized firms have conflicting or competing goals as well as different risk preferences (Eisenhardt, 1989).

To manage principal-agent relationships, agency theory suggests government should write complete contracts (e.g., laws and regulations) that adequately protect public interests and prevent privatized firms' opportunistic behaviors. Furthermore, relevant existing laws or regulations that apply to the privatized firms should be specified by every privatization deal, and enforcements of the contracts should be followed (Ramamurti, 2000). In reality, in some cases, it is difficult and costly to identify all potential opportunistic behaviors and write complete contracts because agency theory assumes that individuals are boundedly rational (Eisenhardt, 1989; Williamson, 1996). In other cases, increases in incentive alignment between government and privatized firms may be a way to reduce the likelihood of opportunistic behaviors (Dharwadkar, George, & Brandes, 2000). Because agency theory assumes that individuals are self-interested (Eisenhardt, 1989; Williamson, 1996), a country should have effective control mechanisms (e.g., contracts, regulatory systems and enforcement) to prevent and solve agency problems.

Agency theory also assumes that individuals are risk averse (Eisenhardt, 1989), suggesting that privatized firms may assume higher risks or costs for engaging in opportunistic behaviors against their government especially in cases that effective monitoring and control mechanisms are in place. For instance, to prevent opportunistic behaviors, Mexico and the Philippines made the sale of SOEs transparent by adopting competitive bidding procedures, developing objective criteria for selecting bids, and creating a clear focal point with minimal but necessary bureaucracy to monitor the overall program (World Bank, 1992). In essence, governments can manage principal-agent problems through effective control mechanisms such as company laws, disclosure provisions, appointing non-executive directors, internal and external audit systems, and so on (Heath, 1997).

*Proposition 5. The more effective a country's regulatory systems are, the less likely the privatized firms will behave opportunistically.*

## **Resource Based View**

The resource-based view (RBV) explains the specific characteristics of resources that are most likely to create and sustain competitive advantage to an entity (e.g., a firm or a country) (Barney, 1991). RBV theorists argue that: (a) resources that are valuable and rare can lead to the creation of competitive advantage; and (b) the competitive advantage can be sustained over longer time periods to the extent that the entity is able to protect against resources being imitated, transferred, or substituted (Barney, 1991; Black & Boal, 1994; Wade & Hulland, 2004).

In business, resources can be defined as tangible (e.g., machines) and intangible (e.g., software patterns) assets and capabilities (e.g., technically and managerial skills) that are available and essential in detecting and responding to market opportunities or threats (Sanchez, Heene, & Thomas, 1996). In the context of a country, resources may refer to assets and capabilities that are available and critical in creating and sustaining a nation's competitive position in the world. Countries actively compete for resources and capabilities that contribute to building their national competitiveness economically, politically, and militarily. From a RBV perspective, in order to create and maintain national competitiveness, a country should not privatize any critical assets and capabilities, such as nation's historical heritage, valuable human capital, scarce nature resources, unique and essential services, military, and so forth. When a country possesses critical resources and capabilities that are both imperfectly mobile and generalizable (Leiblein, 2003), the nation's competitive position can be sustained. Society as a whole, in turn, benefits.

*Proposition 6a. The more critical assets and capabilities are to a country's competitiveness, the less likely the country will privatize them.*

For non-critical resources, the key issue is whether or not the resources can be utilized cost-effectively and socially responsibly. In business, to create competitive advantage, firms must generate more value from its resources than expected at the time of their acquisition or development (Leiblein, 2003). At the country level, if a country is not able to enjoy an economic rent effectively from its resources in one sector, the country is more likely to free the resources for opportunities with higher rents. Thus, the government is more likely to initiate privatization in this sector in a socially responsible way. If, in the same sector, the remaining SOEs are not able to generate economic and social values from their resources (e.g., return of assets, community involvement) above and beyond the value yielded by those private firms with the same resources, the country is more likely to further free the resources from these SOEs for better opportunities in the market. The entire sector may end up undergoing full privatization of ownership. The success of privatization from this one sector is more likely to encourage its government, in order to capture full utilization of its resources, to embrace privatization in other sectors, or, perhaps, all sectors managing non-critical resources. On the other hand, failures from its initial attempts to privatization may lead to a country, in order to reduce opportunity costs, to seek other alternatives (e.g., partial privatization of ownership) or nationalization. In essence, privatization provides a means for government to utilize its non-critical resources cost-effectively and in a socially responsible way.

*Proposition 6b. SOEs, that manage non-critical resources and that underperform economically and socially, are more likely to be privatized.*

### **Transaction Cost Economics**

Transaction cost economics (TCE) describes an entity (e.g., a firm, a country) as an efficiency-inducing administrative instrument that facilitates exchange between economic actors (Leiblein, 2003). Transaction costs, apart from production costs, are costs in relating to facilitating and completing an economic exchange. From a TCE perspective, privatization is an economic exchange in which the sum of total transaction and operation costs should be minimized (Williamson, 1979). Transactions costs have been used to explain government choice in the decision to contract out (e.g., Hefetz & Warner, 2004; Nelson 1997; Sclar 2000). In the privatization case, transaction costs, in addition to costs incurred in designing privatization programs, establishing regulatory systems, and monitoring and enforcing the implementation of the programs, include costs relating to possible social and political problems. Moreover, government transaction costs of intervening in operations and some decisions of the firm are generally higher when firms are privately owned (Megginson & Netter, 2001). Therefore, policy makers should carefully examine privatization transaction costs, because they are not purely economic, but also include potential, delaying social and political costs.

TCE theory, similar to agency theory, also assumes that individuals are boundedly rational and self-interested (Williamson, 1996). Facing uncertain environment and unforeseeable outcomes of privatization, boundedly rational policy-makers find that it is difficult to design a perfect privatization program, write complete contracts and regulations, and monitor the program effectively. Moreover, some opportunistic exchange actors (i.e., privatized firms) may seek short-term economic gains at the expense of social justice for those most affected (Prizzia, 2001), especially when incentives for long-term sustainability and social performance in contracts are weak and monitoring and control mechanisms are insufficient. The complexity of privatization and unpredictability of its outcomes create potentials for opportunistic behaviors, which, in turn, increase its transaction costs (Williamson, 1979). Government, however, may be better off when promoting a free market and introducing competition, because both the increased number of privatized firms and heightened competition among firms can lead to decreased tendencies of engaging in opportunistic actions and shirking behaviors (Shook, Adams, Ketchen, & Craighead, 2009). Furthermore, competition drives private firms to be more competitive and place great pressure on all remaining SOEs to improve their efficiencies as well as on government to reduce



interferences in its economy. Consequently, transaction cost is lower as monitoring cost decreases. Furthermore, lower transaction costs lead to minimization of total costs which, in turn, are a driving force for a country to further deregulate and privatize.

However, privatization is a complex phenomenon that involves many uncertain and unpredictable variables prior to, during, and post privatization. Governments face issues of how to implement privatization programs successfully and to achieve desirable outcomes. TCE may provide insights in that simple market contracts generally provide a more efficient, or lower cost, mechanism for managing economic exchanges than hierarchical organization (Leiblein, 2003; Williamson, 1996). In this regard, a government should design simple, sequential privatization programs and manage the programs through feedforward, concurrent, and feedback control mechanisms. Moreover, a government should create a minimal but necessary bureaucracy to monitor and modify the programs in a market economy. If a government discontinues its ambitious privatization programs, modifies the programs at a large scope, or creates excessive bureaucratic agencies to monitor the programs, the transaction costs may increase substantially or even surpass the economic and social values provided by the privatized firms. In such cases, as Williamson's (1971) suggestion of vertical integration in business, partial privatization or parallel market (e.g., Joseph, 2010; Ramamurti, 2000) may be a more effective alternative.

*Proposition 7. The higher transactional costs of privatization a country perceives economically, socially, and politically, the less likely the country will undergo privatization.*

## DISCUSSION

Through the lens of seven organizational theories, this study offers a conceptual framework to foster future research in privatization. Given the complexity of privatization, multiple theoretical perspectives are vital to enrich our understanding of such a phenomenon. From a management perspective, I attempted to address questions such as why a country undergoes privatization only in some industries and why some countries enjoy success but others experience failures.

This study, built on multiple theories, may provide complementary insights. Contingency theory emphasizes a pragmatic way of privatization. The resource-based views offer insights into what to privatize and real options theory suggests how to privatize, whereas institutional theory and agency theory propose mechanisms for managing and monitoring privatization. Further, TCE provides perspectives that privatization may be a means for a country to improve its economic efficiency and social responsibility, thus enhancing its competitiveness in the world. Together, they may be under the tenets of systems theory, which views a country as an integrated political, social, and economic system, and suggests the success of a privatization program is dependent on how well the system moves (i.e., correcting errors) toward increasing compatibility between the system and its environment.

In addition to the complementary views, this study suggests some of the theoretical implications may be contradictory. For example, TCE suggests that a country should privatize enterprises or industries if the sum of total transaction and operation costs is minimized, whereas resource-based view emphasizes that a country should not privatize enterprises or industries that involve critical resources and capabilities affecting the society significantly or contributing to its national competitiveness in the globe. Similarly, Institutional theory implies that a country may imitate other countries' successful privatization programs in an uncertain environment, whereas contingency theory stresses a customized privatization program contingent upon the country's unique environment.

These complementary and competing implications suggest that future research needs to examine privatization in greater depth and develop studies derived from a synergistic framework of multiple theories. In addition to a multi-theory perspective, a multi-level (i.e., country-, industry-, and firm-level) analysis may enrich our understanding of privatization. Both the complexity of the context in which privatization occurs and the means through which it is implemented require that the phenomenon be analyzed from a multilevel perspective (Ramamurti, 2000). In terms of examining the effectiveness of

privatization, this study emphasizes that, in the case of privatization, economic efficiencies should not be at the expense of social or political cost. Future research may benefit from examining privatization outcomes both economic and social performance in a long run (Prizzia, 2001).

Future research may also focus on other privatization questions. For example, some scholars argued that timing of privatization is a critical issue to its success (Brada & Ma, 2007; Taylor & Warrack, 1998). This study, however, did not directly address the question of when to privatize. Indirectly, this study offers some implications with regard to the timing issue, such that a country should: (a) be well prepared before launching its privatization in the sense of a well designed program and a readily competitive market; (b) examine sequencing and staging issues of privatization; and (c) balance between its privatization choice and adaptation to its environment over time.

In conclusion, this study makes an attempt to systematically look into privatization from a multi-theory perspective. By viewing a country as an integrated political, economic, and social system, the study offers a broad conceptual framework for researchers and policy makers. Such a framework provides insights into: (a) why to privatize—from the tenets of systems theory; (b) what to privatize—from the perspectives of contingency theory, resource based views, and transaction cost economics; and (c) how to privatize—from the frames of the real options theory, institutional theory, and agency theory. This study advocates a broad, systematic view of privatization and careful and meticulous attentiveness to its long-term consequence to a society.

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**APPENDIX**

**TABLE 1  
IMPORTANT THEORIES AND IMPLICATIONS FOR PRIVATIZATION**

Theoretical Perspective	Key Premise	Key Insights for Privatization	Propositions
Systems Theory	Public and private organizations are viewed as components of a country's integrated political, social, and economic system.	<p>A country's system is viewed as an open system that is affected by both external (from a global perspective) and internal (within a country) factors.</p> <p>Public and private organizations, government, and the general public are components in a country's system that are open to, and interact with, their environments.</p> <p>Feedforward, concurrent, and feedback control mechanisms are essential for a country to manage sequencing and staging of privatization.</p>	<p>Proposition 1a. The stronger global competitions countries face, the more likely a country will undergo privatization.</p> <p>Proposition 1b. The less efficient SOEs are, the more likely a country will undergo privatization.</p> <p>Proposition 1c. The more important industries are to a country's economy and social welfare, the less likely these industries will be privatized in early stages of privatization.</p> <p>Proposition 1d. The better sequencing and staging of privatization are managed, the more successful privatization will be.</p>
Contingency Theory	There is no universal or one best way to privatize.	<p>The effectiveness of privatization depends on proper fits:</p> <ol style="list-style-type: none"> <li>1) between a privatization program and a country's internal and external environment;</li> <li>2) between subsystems and a country's environment; and</li> <li>3) among subsystems within the environment.</li> </ol>	Proposition 2. Countries developing their privatization programs contingent upon the country's environment are more likely to succeed than those who do not.
Real Options Theory	A real option is the right choice, but not the obligation, to undertake privatization in an uncertain environment.	<p>Privatization programs create economic values through operating flexibility.</p> <p>Privatization programs should be evaluated periodically. Modifications and improvements should be followed.</p>	Proposition 3. In uncertain environments, countries, who undergo privatization with a wide range of options and manage it with flexibility, are more likely to succeed than those with a single, rigid privatization option.

Institutional Theory	Social structures, including rules, norms, culture and values, guide people's social behaviors.	<p>An effective and efficient institutional system is critical to the success of privatization.</p> <p>A country should not simply imitate other countries' successful privatization programs.</p>	<p>Proposition 4a. Countries who pursue privatization and institutionalization simultaneously are more likely to succeed than those who pursue one without the other.</p> <p>Proposition 4b. The more uncertain a country's environment is, the more likely the country will imitate other countries' successful privatization programs.</p>
Agency Theory	A country should use monitoring and control mechanisms to manage principal-agent relationships.	<p>A country must have effective control mechanisms (e.g., laws and regulations) to prevent agents' opportunistic behaviors.</p> <p>The costs of monitoring private sectors are part of the transaction costs.</p>	Proposition 5. The more effective a country's regulatory systems are, the less likely the privatized firms will behave opportunistically.
Resource Based Views	Critical assets are sources that a country should not privatize.	<p>A country may create and sustain national competitiveness by maintaining critical resources.</p> <p>Privatization provides a means for government to utilize its non-critical resources cost-effectively.</p>	<p>Proposition 6a. The more critical assets and capabilities are to a country's competitiveness, the less likely the country will privatize them.</p> <p>Proposition 6b. SOEs, that manage non-critical resources and that underperform economically and socially, are more likely to be privatized.</p>
Transaction Cost Economics	A country should make privatization decisions that improve its economic efficiency and society as a whole.	<p>Privatization is an economic exchange in which the sum of total transaction and production costs is minimized.</p> <p>Laws and regulations should be in place to prevent opportunistic behaviors.</p>	Proposition 7. The higher transactional costs of privatization a country perceives economically, socially, and politically, the less likely the country will undergo privatization.