

**ADDIS ABABA UNIVERSITY
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**THE MACROECONOMIC IMPACTS OF PRIVATIZATION IN ETHIOPIA: A
TIME SERIES ANALYSIS**

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**THE MACROECONOMIC IMPACTS OF PRIVATIZATION IN ETHIOPIA: A
TIME SERIES ANALYSIS**

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Abstract

This study attempts to assess the macroeconomic impacts of privatization in Ethiopia using the data for the 1994-2018 period focusing on the growth, fiscal, and debt relations. The main objective of the study is to examine the growth impacts of privatization directly and in relation to the private sector development and boosting trade openness by overcoming the previous studies data and methodological problems. After a simple economic growth model of real GDP growth as a function of privatization proceeds, private sector contribution, government debt stock, trade openness, and government consumption, all econometric tests have been conducted properly. All tests directed towards the econometric estimation method of error correction model to be employed. The correlation analysis of whether privatization is justified by the debt conditionality by the international and multilateral organizations and by the huge national budget deficit is computed. It is found that privatization highly and significantly correlated with a national budget deficit but insignificantly with debt stock. But it is found a statistically significant Granger causality running from debt to privatization implying there is debt conditionality for privatization in Ethiopia. The empirical evidence suggests that the debt stock affects economic growth negatively both in the short run and long run indicating the debt overhang problem of the country which is a possible cause of privatization that does not have a long-lasting growth impact. The private sector development has found insignificant to the economic growth of Ethiopia as proposed by the privatization program and other policies. Private sector contribution affects economic growth negatively and only significant in the long run. The level of international competitiveness measured by trade openness has found a significant positive growth impact in the short run and but insignificant in the long run. This shows the crucial role of competitiveness in the country. The empirical Granger causality test shows there is no causality between competitiveness and privatization that could impact economic growth by enhancing the efficiency gain. Therefore the positive economic growth impact of competitiveness comes from the country's trade potential and not by the policy of privatization.

Keywords : privatization, efficiency, competitiveness, error correction model, growth, private sector contribution

Declaration

This is to certify that the dissertation prepared by Mengistu Alamneh entitled "THE MACRO-ECONOMIC IMPACTS OF PRIVATIZATION IN ETHIOPIA: A TIME SERIES ANALYSIS" and submitted in partial fulfillment of the requirement for the degree of Master of Science in economic policy analysis for the graduate program complies with the regulations of the university and meets the accepted standards with respect of originality and equity.

Signed by the examining committee:

Examiner _____ Signature _____ Date _____

Examiner _____ Signature _____ Date _____

Principal supervisor _____ Signature _____ Date _____

Chair of Department or Graduate Program Coordinator

Acknowledgment

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Chapter 1

Introduction

1.1 Background of the Study

In the long history of Ethiopia, and specifically, the near recent three of Imperial, Derg, and EPRDF regimes of the nation scored cyclical economic growth with cyclical macroeconomic policies. Economic growth in Ethiopia is highly determined by the political factors, vagaries of nature, strength, and efficiency of institutions, the efficiency of public policies, international commodity prices, and risks related to instability and property rights. According to Degefe and Geda (2005), Ethiopia has been developing national development policies for more than three-fourths of a century. The first five-year national development plan was issued in the mid-1950s by the Imperial Ethiopian government and was followed by four others until the mid-1970s. The Military regime that toppled the Imperial regime followed suit, first by annual plans culminating with the ten-year indicative plan issued in the mid-1980s. The Ethiopian People's Revolutionary Democratic Front (EPRDF) government developed two five year plans. Currently, the government claims to have generated a "Home Grown" plan under the auspices and assistance of Bretton Woods Institutions.

The history of privatization starts with the government of EPRDF reversing and undoing the socialist bent policies of the military regime as soon as it assumed power in the early 1990. The military regime initiated wholesale nationalization of what it considered "commanding heights" of the economy in the 1970s. The privatization drive was initiated by EPRDF as part of an agreement it had with the Bretton Woods institutions for financial assistance followed by the HIPC arrangement of debt reduction and commitment to reduce poverty by half by 2015. Privatization is the most tangible of the manifestation of the withering of the state required by the Washington Conesus (see Cramer, 1999) where 70 percent of structural adjustment loans made during the 1980s contained privatization (see cook and Kirkpatrick, 1995) of which has

been most prominent for sub-Saharan Africa(see Bennell, 1997).

Theoretically, privatization is argued in support of boosting internal and external competitiveness through increased efficiency. In addition, Privatization was expected to boost economic growth by attracting and redirecting both domestic and foreign investments; which is becoming the most important source of finance for developing countries. According to Selvam (2007) privatization affects investment through three channels. Firstly, privatization causes capital inflow since following the purchase of public enterprises by foreigners who may then proceed to capacity expansion, modernization, and renovations of the already purchased enterprises. Secondly, privatization if well managed has had a positive correlation with domestic and foreign investments. It has reduced the crowd out effect and provides credit for the private sector. Thirdly, privatization may help the government to re-invest on the existing and divested enterprises. The benefit from such investment reduces fiscal distress on the government and gives it the capability to provide more attention to the productive sectors. In creating markets and increasing private sector participation, market constraints should be addressed in ways that lead to attractive investment opportunities for the private sector, while also delivering continued poverty reduction and inclusiveness.

Privatization may be undertaken in different modalities, depending on various socio-political and economic factors, including their level of development, the political slant of the government, international debt, the levels of economic and institutional development, and enterprise-specific factors. Thus privatization may be undertaken via restitution, management-employee buyouts (MEBOs), and lease buyouts. In recent years voucher privatization has grown more popular. The effect of privatization, in turn, depends on the method of privatization. The capital market development and distribution of wealth with managerial ability have a significant effect on growth effect relative to modalities of privatization. If there is a well-developed capital market, entrepreneurs have access to credit and are able to participate in the purchase to lead privatized firms with innovation.

Privatization is not to be undertaken to close the budget gap-i.e. for fiscal therapy. Rather it is a redeployment of assets in the economy from the public sector, presumed to be inefficient, to the private sector, where it is used more efficiently. Privatization, thus defined unequivocally as the shift of assets and functions from the state to the private hand. Such transfers are, by their very nature, politically sensitive and subject to corruption and abuse (see Estrin and Pelletier 2018). By its simple transfer, privatization cannot bring the stated objective of improving the economic and financial performance of enterprises. The tradeoffs between the quality and access of the privatized enterprises product or service, and other economic gains of price decline,

employment, profitability and out-put must be considered and included in the appraisal analysis of the policy. This can be reconciled by developing strong and prudent regulatory frames and institutions that both are lacked in developing countries. Therefore, privatization for developing countries like Ethiopia is externally loaded and unlikely to generate growth and reduce poverty. Markets are not institutions; however, they need the smooth functioning of other institutions to contribute positively to economic growth (see Degefe and Geda, 2005).

In addition to the efficient use of scarce resources, there are many other factors, which determine the rationale for privatization. Among these are serious domestic economic crises, shortage of foreign capital, and high dependence on international agencies like the World Bank and IMF. When many African countries adopted the Structural Adjustment Program (SAP) in the 1980s, the governments were required by the World Bank and IMF to relinquish state-owned enterprises as one of many conditions for economic assistance (see Guseh 2001, Breen et al 2013). The effects of privatization on the macroeconomic variables are extensively studied. These studies are most of the cross country genre on developing, transitional, and developed countries case. Single country case studies are very rare both in developing and developed countries. Even in these studies (cross-country), the impacts of privatization on the macroeconomic variables of economic growth, unemployment, investment, and fiscal stance are inconclusive.

The empirical pieces of evidence on the macroeconomic impacts of privatization in developing countries resemble the insufficiency of private ownership alone. Estrin et al (2018) reviewed the existing empirical studies in developing countries and concluded that developing countries should focus on the following conditions. Pre-conditions especially regulatory infrastructure, an appropriate process of privatization and well designed and sequenced reforms with strong public communications are important for attaining positive impact. From here, it is clear that not the economy but also the process of privatization needs a strong and powerful government. But, these conditions are lacked by developing countries that make privatization an ineffective policy in developing countries.

1.2 Statement of the Problem

The policy issue of privatization, despite the dozens of empirical pieces of evidence in its support, coincides with the increasing dissatisfactions among the public and policymakers. The dissatisfaction about privatization arises from the growing questioning of the benefits of privatization and attempts to convince its role as a panacea for all economic problems. The successes are in broader socially and politically competing objectives, where their realization is subject to some local conditions such as proper policy and regulatory frameworks. Thus, it inclined from the stated macroeconomic and distributional gains. This is an undesirable policy or type of growth even if it did, for countries like Ethiopia where the distribution of income and socio-political thoughts are ethnic-based.

The privatization efforts of most developing countries are inhibited by embryonic financial markets, weak regulatory capacity, and a public sector that accounts for a large share of GDP (see Boubakri and Cosset, 1998). But some of these countries have large markets and fast economic growth rate features that make the success of government divestiture more likely. On the other hand, many, particularly those with low per capita income, lack some of the main ingredients for successful privatization, such as capital, entrepreneurs, and competent managers. On the other hand privatization to stimulate competition for the expansion of export that has a pace for growth by enhancing efficiency and generating foreign exchange needed for development activities. In this conception there should be a link between privatization and trade openness-competitiveness. Thus, is there any relationship between privatization and competitiveness situation which could be affected on economic growth?

The method and way of privatization policy implemented in developed countries should and could have resulted in different results in developing countries, where the local conditions are almost completely different. Despite this, privatization is proved empirically in most studies in its positive post-privatization performance improvement. This has been shown positive changes in terms of lowered costs, improved labor efficiency, increased outputs, higher dividends, and very often increased investment post-transaction. The potential reasons frequently stated to explain these results include; government giving the company a monopoly position, or awarding it some other cost-reducing concession in terms of the policy, tax breaks, exemptions from customs duties or social security payments, or special deals on input pricing. Such type of improvements could not be taken seriously since it is at the expense of society. This makes the community feel as they are poor and privatization has to pave the way for monopoly and foreignization that proceeds to strikes and riots. There is no empirical study that addresses the

effect of foreignization and capital flights via foreigners during and post-privatization time.

Privatized firms perform better than public firms in revenue collection but not in cost reduction (see Frydman et al 1999). This revenue improvement is sometimes at the expense of the community by a price increase, limiting provision or production for the non-profitable groups and ignoring the poor. Therefore, in countries where transaction costs are high in the process of contracting, the cost of organizing the bidding process, monitoring contract performance, and enforcing contract terms introducing competition has a better outcome than privatization. Kikeri (1998) points at the circumstance where as a result of the privatization process prices increase and employment as well as tax payments decrease. In that case, poverty will only be aggravated. Introducing competition to the public may improve than privatization securing the public's interest.

Privatization in Ethiopia has been undertaken for three main reasons according to the privatization of public enterprise proclamation 146/1998. This includes: generating revenue required for financing development activities undertaken by the government, changing the role and participation of the government in the economy to put its attention in the needy ones, and promoting the country's development by promoting the participation of the private sector. Taking this into consideration, Selvam (2007) grouped the reasons for privatization in Ethiopia as follows. First, the country's high fiscal pressure due to huge public debt and external debt forced the government to privatize. Second, dependence on loans from international organizations narrows the revenue options. Third, a large share of investment in state-owned enterprises forced the government to privatize and reduce its investment burden. And last but not least, the poor performance in terms of productivity and profitability constrained its prospect for the long-run growth.

The evidence shows that the actual effects of the privatization process in LDCs do not correspond with its theoretical outcomes. The expectations with respect to the results of privatization are based on studies conducted in the West but these studies fail to take the contextual factors of LDCs into account (Redda, 2007). These factors are generally described as country and market conditions, as discussed above. Despite the small number of studies found on the growth and private capital formation effects of privatization on a single country case, the macroeconomic (growth and capital formation) impacts of privatization in Ethiopia are inconclusive. Among these, Selvam (2004, 2007) made a causal analysis. He did also a regression based on heterodox model specification for 10 years of data and found a negative relationship between privatization and private capital accumulation and also with total investment. In the first place, this study is outdated and should be updated.

The second study is by Reddy and Desalegn (2018) which is the most recent. In this study, they used 23 years of semiannual data measures applying ARDL regression and found a positive short-run and long-run relationship between privatization and economic growth. This study didn't acknowledge the previous study result in overcoming the previous short comes. On the other hand, the primary limitation in this study (even though accredited as their limitation) is the semiannual data use in a nation where rain feed agriculture is a dominant source of GDP.

Privatization is undertaken sporadically (Cook and Uchida, 2003; plane, 1997). According to the Ethiopian Privatization Agency, privatized firm owners are required to pay 35% first. This creates dalliance on the collecting process and as Cramer (1999) said privatization is sensitive to political abuse, corruption and weak in its implementation that weakens the logic of using semiannual data that leads to the wrong result and conclusion based on this. Privatization affects not only supply but also the demand side of the economy especially when it is home-based. The previous studies are one-sided on supply. In addressing these data and methodological problems, this study will develop a simple growth model that is going to explain the country's economic performance. Then try to answer the question; does privation policy have both short-run and long-run impacts on the growth of the country.

In this study, I used 1994 to 2018, a 25 years annual data. The study also made a correlation analysis between the variables of privatization with national budget, external debt, and private share from national income. In addressing the growth impacts of an economic policy-privatization, it is better to use the time series analysis than the usual cross-countries studies of the panel data method. Because it helps to exploit fully the time lag effects and dynamics of the policy impacts. Accordingly, Levine and Zervos (1993) argue that cross country regression should be viewed as evaluating the strength of partial correlations, and not as behavioral relationships that suggest how much will change when policy changes. The primary motivation for this study is the result difference between the above listed two studies and the increasing plan of privatization in the country with the ever-increasing external pressure.

1.3 Objective of the Study

1.3.1 General Objective

The general objective of this study is to assess the short-run and long-run impacts of privatization on the economic growth of Ethiopia.

1.3.2 Specific Objectives

In the privatization policy of Ethiopia, the government had set three main objectives to achieve using it as stated above. To address this, the government is overwhelmingly privatizing state-owned enterprises. Therefore, this study sets the following specific objectives in assessing the macroeconomic impacts of the policy.

- Check the long-run co-integration between privatization and economic growth of Ethiopia
- Examine the correlation between privatization and national budget deficit in support of the privatization's reasons of fiscal pressure
- Examine the growth effect of competitiveness of the country in relation to privatization
- Examine the role of the private sector share in the economic growth of Ethiopia
- Analyze the correlation between privatization and foreign debt in support of the external pressure from IFIs for privatization

1.4 Hypothesis of the Study

Taking the previous studies and theoretical explanation of economic growth and privatization, this study will test these three hypotheses:

- H₀: there is no long run co-integration between privatization and economic growth
- H₀: the private sector development does not have a long run economic growth impact
- H₀: privatization and national budget deficit does not have any correlation

1.5 Significance of the Study

The policy issue of privatization has generated heated debate among economists, policymakers and even the public, dividing the participants into two groups on its desirability. On the one hand, privatization is taken as one of the policy tools for transferring unproductive resources to the productive-private sector. State-owned enterprises are inefficient than private, and privatization is a reallocating mechanism. On the other side of the group, privatization is externally squashed policy (see Adam et al., 1992, Hemming & Mansoor, 1988,) of Washington consensus via its organizations of the World Bank and IMF. In the meantime, the dispute in the ways that micro benefits are transferred to the macro or did privatization has a direct positive impact on employment, production growth, welfare improvement, and fiscal and financial performance improvement is not the uncovered truth. Even if there are dozens of researches in the area, almost all are in a cross-countries level that lacks the country-level effects. This study, therefore, will address this issue and will be one layer that adds up on the area of single country study of the effects of privation on economic growth in developing countries and in Ethiopia particularly.

1.6 Organization of the Study

The remainder of the paper is organized as follows. Chapter two deals with the theoretical literature and empirical literature review proceeded by chapter three of descriptive analysis and trend of privatization in Ethiopia. In the fourth chapter, a theoretical model specification is presented and then the empirically estimatable econometric model is developed. The full data sources and econometric tests description is also included. Chapter five followed with econometric results discussion and the paper will be closed with chapter six's conclusion and some policy implications.

Chapter 2

Survey of Literature

2.1 Theoretical Literature Survey

The theoretical principle of privatization more resembles to the microeconomic benefits of the policy mediating other contributions to growth and development via economic efficiency and allocating scarce resources from the public inefficient to the private efficient use. This principle is generally theorized in three core theories. The principal-agent theory, property rights theory, and the public choice theory. Now let's see the definition and come back in detail. Ethiopian government-defined privatization in the 1998 privatization proclamation as "Privatization means the transfer, through sale, of an enterprise or its unit or asset or government shareholdings in a share company to private ownership, which includes the making of an enterprise a government contribution to a share company to be formed with participation of private investor and privatization of the management of an enterprise." Therefore, privatization is the transfer of some or full ownership from the public to the private. Thus, the Ethiopian government definition shares other international and regional organization definitions.

The Organization for Economic Corporation and Development (OCED) defines privatization as "any material transaction by which the state's ultimate ownership of corporate entities is reduced". Filipovi (2005) shortly defined as "a method of allocation of assets and functions from the public sector to the private sector". Whereas Merriam Webster dictionary defined as "to change from public to private control or ownership" and first known used in this definition since 1948. In general, all definitions take in common the transfer of assets or functions from the public to the private either partially or fully.

The property rights theory of privatization makes one crucial assumption on the different private and public holdings of assets or some sort of functioning. The core point in the theory is the ease of handling, enhancing, managing and transacting of assets in the private than

the public. Ownership matters more according to this theory. On the other way, government managers do not organize inputs in a way that maximizes the wealth and welfare of the general citizenry. That is the public is inefficient and managers enjoy the quitters' lives. Property rights are instrumental in achieving both allocative and productive efficiency with respect to the use of firm resources (Vickers & Yarrow, 1988a cited in Redda, 2007). The property rights theory seems to indicate that (1) private production is cheaper than production in publicly owned and managed firms. (2) But given sufficient competition between public and private producers (and no discriminatory regulations and subsidies) the differences in unit cost turn out to be insignificant. From this one may conclude that it is not so much the difference in the transferability of ownership but the lack of competition that leads to the often observed and less efficient production in public enterprises.

The principal-agent theory focuses on the core idea of corporate governance. Despite the problem of interest divergence is common both in private and public enterprises, it is much lesser in private enterprises (Schneider, 2003). Agency theory sees privatization from the divergence of interest point of view. A manager acts out of self-interest and ignores the owners' interests. Therefore privatization gives an incentive that motivates the manager to adjust its interest to the enterprises better than the public owned.

The third public-choice theory stands on "The politicians, bureaucrats, managers of public enterprises are selfish utility maximizers subject to constraints" (Schneider and Frey, 1988, cited in Schneider, 2003). According to public choice theory, the performance of public enterprises is determined by the combined actions of the general public, politicians, bureaucrats and managers, each group seeking to maximize their own particular objectives (which may not coincide with efficiency) and none having identical information, with the end result being the internal inefficiency of the firm (Andic, 1992 cited in Chole, 1993). In a competitive environment, however, there is almost uniform access to information, contributing to greater efficiency.

The essence of privatization theory is that the process streamlines the relationship between enterprise owners and managers, and thereby improves performance. There are two main theoretical strands from which more detailed arguments follow. Firstly, according to property rights theory, a private owner, with the right to residual income (profit), will exercise greater monitoring effort than a public sector counterpart with no such direct rights. Secondly, public choice theory in the New Political Economy tells us that privatization reduces the scope for manipulation of an enterprise for political (and inefficient) ends. Privatization simplifies the relationship between the agent (i.e. an enterprise manager) and principal (a shareholder in a private company or the government in a state company) (Cramer, 1999).

2.2 The State in the Economy

It is informative to see the status of the state in the economy to shed light on the reverse move to the private sector or market lead-capitalist system through privatization in developing countries. Handfull studies conclude that privatization is the reverse of one-time nationalization or reducing of the ever existing. In the common goal of reducing poverty and stimulating economic growth, in the 1980s developing countries experienced a reversal of the previous two decades during which the public sector was seen as playing the dominant role (Friesel et al 1991). In the aftermath of colonial time, the African economy was a public lead. But the 1980s and 1990s world crises and debt stress of the continent eliminated its options but to fall on the hands of the westerners and IFIs. African privatization reasons are quite different from others like Latin American which was mainly the overused state enterprises and the overgrowth of the private sector and its readiness to hold tasks while the former was externally imposed before countries ripe for privatization (Ramamurti, 1991).

There is no common demarcation on the share and power of the state in the economy, at different times and circumstances. Again there is an ambiguous global trend towards reducing government business ownership, but this trend has been slowed or reversed in or through the 21st century (Megginson, 2017). According to Megginson, there are seven major themes in the analysis of privatization and state business ownership. These themes are features that create the ambiguity in the discourse of whether state power has been declining or increasing through time.

The first theme is the Chinese rise up as the global economic power and a competing model of business ownership and organization. The Chinese GDP in 2000 was US \$1.22 trillion, representing 3.6% of the world GDP, while in 2015 US \$11.06 trillion and 17.52% of world GDP at market price respectively. China in this time is becoming the world-leading exporter, a leading manufacturer, and a leading economy in purchasing power parity measures. The other feature in the Chinese's economy is reliance on and support/influence for the large state-owned companies in the business and growth champion has prompted the observers to group it in the "state capitalism" category. Countries like Brazil, India, Russia, and Singapore has raised global prominence by the state-owned or highly influenced businesses. This is one manifestation of the state power increase and privatization or capitalists' free-market policy reversion.

The second theme, Megginson raised is, Outside of China—and Russia—state ownership of business assets has increasingly taken the form of portfolio equity investment by governments and state-owned investment funds, rather than direct ownership/operation of state-owned en-

terprises. Megginson claims that the state asset is increasing and not decreasing in many aspects. But it seems that Megginson is talking about developed countries. Amongst this, the government equity purchase from the private sector has risen than the privatization proceeds. He supported this by data as in the period 2001-2012 governments actually acquired more assets through stock purchase-which is \$1.52 trillion than they sold through share issue privatizations. At the same time, direct sales amount to only \$1.48trillion. Thus, this world is undertaking two contradictory things of privatization and nationalization simultaneously. This becomes another stimulus for developing countries to take it serious privatization could result in paving the way for the scramble of Westerners like the colonial time.

Thirdly, in the middle inngs of (2005-2014) the progressive world oil price increase shifted power and wealth to the (most) non-democratic petroleum exporting nations and to their wholly state-owned national oil companies. On April, 2018, Bloomberg released saying the state-owned Aramco Saudi oil producer unveils the financial secret of the world's ever most profitable firm outstripping the US firms of apple inc. and Exxon mobile corp. The radical oil price rise of the period, as the price rise from 25\$ per barrel to 147\$ per barrel in 2008 and the average price of \$100 in the period of 2010-2014 multiplied by the period average production of 90 barrels per day, enriched a set of countries. These rentier economies dominated by state-owned enterprises and gave unprecedented sway over the world's most important commodity. But the 2014 third-quarter oil price decrease and the continued decline seems like the global economic power changer and probably a surge in the privatization of the formerly sacrosanct NOCs, beginning with Saudi Aramco in 2018. Thus, the global trend of the state-private proportion or takeover is dynamically changing and is out of perfect prediction.

The fourth theme, Megginson raised is the world financial crises of 2008/9; governments' subsequent policy responses reversed the state intervention norm at least temporarily. This trend continued to the less government intervention in and ownership of a business in the long-run. Following Lehman's brother bankruptcy in the US, the 2008 financial crises erupted and warned/enforced many governments to take some action in rescuing the banks and other financial institutions to nationalize at least partially in the process. The time's nationalization of the US through the large purchase makes the US the largest privatizer of 2009-2012, and other countries make it the long-run trend to unwind the process. Megginson argues that in the immediate response to the crisis, the world's major central banks flooded markets with liquidity and sharply lowered interest rates, and later embarked on a series of increasingly unorthodox actions—particularly quantitative easing—designed to rekindle economic growth and avoid deflation. The financial distortions and record low-interest rates engendered by these

policies endure to the present day, though most of the world's key central banks began modest tightening in 2017.

The other 21st-century phenomenon is the economic and political unity of Europe increased significantly after the introduction of the euro in 1999 and the expansion of the European Union by ten member countries in 2004. But Europe entered an extended crisis and instability after 2011. The Brexit vote of June 2016 is the most commonly listed crisis for the region in the union and the region. The sixth theme raised by Megginson is that privatization has continued and even increased with a changing pattern of from the public offer secondary share of westerns to the varietal methods in the emerging economies-especially china. The emerging economies of Turkey, Brazil, India, and Russia were becoming the dominant privatizers of the second decade of the century. The last one is the change in the asset privatized on the international agenda of the policy. Since 2004 privatization added by far divestment in infrastructures and less of the state-owned assets.

2.3 The Linkages between the Macroeconomy and Privatization Policy

Economic growth in the quest for development in social, political, and institution is at the center of macroeconomics and one of the pillars of a nation's position on the globe. A nation that is developed is presumed (presumed since there are questions today beyond the commonly used GDP increment measure of development) as the nation that has best welfare of the economy in terms of higher income and wealth, low unemployment, high distribution of income (assuming Kuznets hypothesis of the 1960), high investment, better opportunities and superpower in the world's championship. The reality seems that is not true, rather as the Nobel Laureates Joseph Stiglitz said the US the developed nation, is in "of the one percent, by the one percent, for the one percent" scenario. That's in the developed countries of US one percent of the population controls wealth, power, and opportunities. This phenomenon is extended to other developed countries.

It is apparent in turn to notice that countries that have lower incomes will have a lower standard of living, low lifetime, low employment, low quality of public services like education, health, and others. But it seems that the subject economics should to consider the equity and equality of economies which is increasingly becoming part of the subject. According to Mankiw (1995), the average income of the richest countries is ten times as high as the poorest countries. Thus, what is the factor responsible for this much difference is tried to be addressed

in different economic theories and economic policies? Amongst these policies, privatization is at the forefront in its pillars of trade liberalization, fiscal discipline, less government position in the economy and deregulations. Privatization as the transfer of ownership from the public to private has some space in different growth models in terms of the role of institutions and property rights for growth.

The main motive of the governments of LDCs for starting the process of privatization is to gain economic benefits. The objective is to generate additional state revenue, promote economic efficiency while at the same time maintaining the level of employment and reducing the involvement of the government in the management of enterprises. Other objectives are the transfer of ownership to the private sector, introducing competition through economic liberalization, exposing public enterprises to market discipline, developing capital markets and attracting national and foreign investors (Megginson et al., 1994). By achieving these goals government money, otherwise spent on subsidies, will be saved and political and social stability will be achieved through a more balanced allocation of resources. Moreover, there will be more economic growth and new opportunities will be created with respect to employment. The general expectation is a higher output, increasing investment levels, a supply of quality goods and services at low prices, a growing use of modern technology and know-how, higher profits and dividends, more employment and higher salaries, a reduction in leverage, effective corporate governance, financial benefits and a decrease in taxation levels (Makalou, 1999).

Privatization is a fuzzy concept, which evokes a sharp political reaction (Starr 1998). The time, origin and objective of privatization are ambiguous, which is presented by the Western as an alternative to the increasing state power in the economy mainly after the second WW. Privatization was implemented to some extent for returning service to the private market, while the other where for re-allocating resources. In the short run effect analysis of privatization, its fiscal impact is unequivocally increasing the liquidity of the government. Mackenzie (1998) comes to the akin of privatization to bond issues in its short-run impacts on the macroeconomy assuming home privatization.

Privatization doesn't reduce consumption, because unlike taxation it doesn't reduce wealth. Since privatization entails an exchange of assets that do not affect the net worth of the government or reduce that of the private sector, it should be seen as the financing transaction. But the long-run macroeconomic effect of privatization analysis is quite different from the short run. Therefore, the long-run analysis of privatization should be seen in intertemporal calibration. In addition to the privatization proceeds revenues, the government incurs two types of costs. The future income stream has forgone from the privatized enterprises, and the privatization cost of

transactions including management, information cost of preparing and determining the price of the enterprises, agency or office cost since most countries establish a new office to administer it. Thus let's develop an intertemporal theoretical model based on the cost-benefit analysis.

Suppose that the state wants to sale a specific firm's share i at time t through an auction for the private sector. Thus, in a simple financial principle, the value of packages of the firm's shares should be equal to the present values of the stream of net dividends. Suppose again the dividend is net of tax and the whole profit after tax is shared as a dividend. Again using the constant capital rate of return as the discounting rate, the enterprises discounted future net profits to be obtained can be calculated. The government sets a minimum price for the firm prior to the sale and receives the highest bid offered in the auction. Here there might be a difference between the discounted future income streams and the auction offered values. This is what Mackenzie (1998) said the public-private valuation differential or valuation differential. In short, it is the difference between the net discounted future income streams of the government and the value their share will command with the private investors. In this case, we have to consider two things.

The government income includes the auction income plus the future taxable income generated by the private. The cost side includes the sale transaction costs, which include administrative, cost of sale and enterprise restructuring, and the present values of the projected stream of gross profit under the case of the firm remain state-owned. In short, the opportunity cost of privatizing enterprise i . Then the net worth of the government would be the difference between cost and benefit or revenue. Therefore, the valuation of state-owned enterprises has an important implication in the long-run impacts on the fiscal stance. Santos (2007) estimated the difference for the Brazil privatization program and found that about 14% of state-owned enterprises' true value was not extracted from bidders. Mackenzie argues that investors are risk-averse and use a large discount rate and presents less value than the government or the true value.

2.4 World Privatization Trend

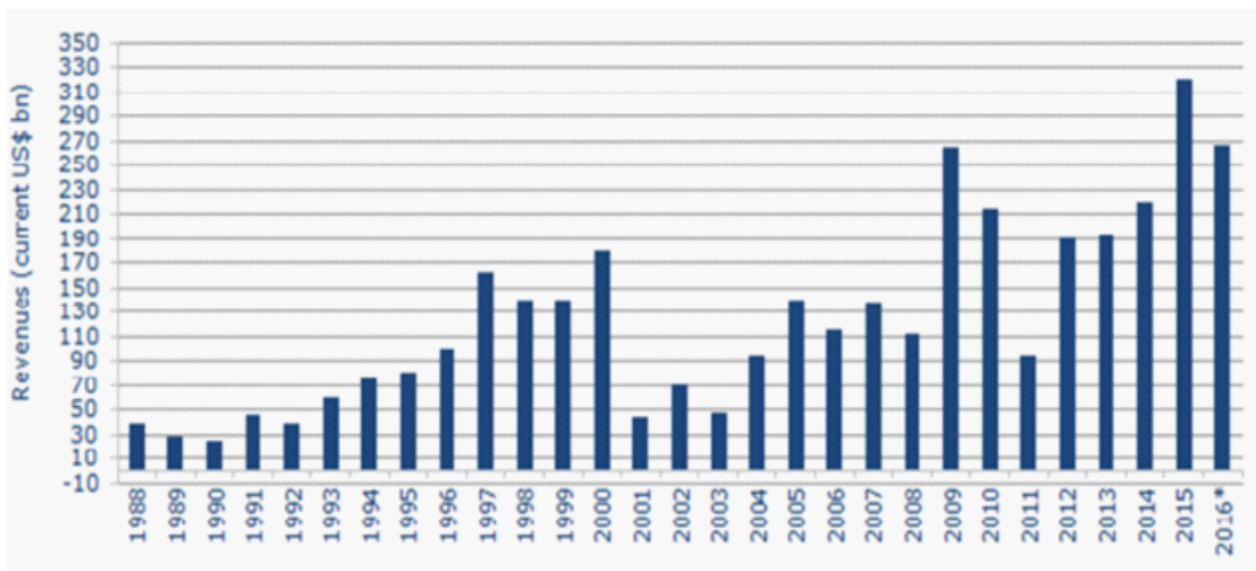
It seems that the economic policy of privatization is evolved since the time of the Republic of Germany, sold the majority of the stake of Volkswagen for private investors. The next big paradigm-shifting policy change was the 1980's Margaret Thatcher's privatization of the Britain telecom. The France Chirac's bank privatization was another striking policy change of the time. Then, it has been sporadically expanded to the other parts of the world such as Japan and Mexico's privatization of large communication services (Megginson et al, 1996). Privatization in the mid of the 1990s reached climax till get dwindled by the 1997 East Asian financial crises and the 1998 Russian debt crises and again revived to after 2002. The relative rise up of proceeds is due to the share sales in telecom, power, and banking sector by the countries China (additional share offering of China Telecom), the Czech Republic (partial sale of Trans gas), Slovakia (partial sale of the electricity company), India (telecoms), Pakistan (United Bank), and Saudi Arabia (telecoms) (Kikeri and Kolo 2005).

The downfall fall of the communist regime in west Europe and the Soviet Union was another tributary to the world privatization revenue rise and seal level ideological changing phenomenon of the time. In recent times China and Cuba have become other implementers for the main objective of stimulating economic growth (Filipovic, 2005). This was transmitted to the Africa region, and specific countries of Ghana and Togo as the starters and Uganda and Zambia joined later (Bhatia et al, 1998). Now a day privatization is almost everywhere and seen as one of the necessary policies of transformation from the state to the private.

In the world trend analysis, Kikeri and Nellis (2004) found that the world private sector share is increasing by the newly entering and the privatized firms. As a result, by the end of the 1990s, the non-state sector share accounted for over 60% of GDP, and the state share in the industrial out-put declined from 78% in 1978 to 28% in 1999. In Latin America, the large scale privatization, especially in infrastructure launched by Chile starting in 1974, raised up the regions that proceed to peak in the 1990s. According to Estrin and Pelletier (2018) between 1988 and 2008, the total privatization proceeds in Latin America amounted to USD 220billion which is 28% of the total world privatization proceeds.

There is a huge proceeds increase both globally and regionally. In a trend analysis Kikeri and Kolo (2005) found that between the time 1990 to 2003, in 120 developing countries, 7860 transactions occurred that generates about USD 410billion that accounts for 0.5 percent of the developing countries' GDP. In the OECD report of 24 sampled countries, the privatization proceeds were USD 487 billion within eight years of the time 2000-2007 reaching a peak of USD

103 billion in 2005. France, Germany, and Italy in combination accounted for almost half of the proceeds of the time about USD 233 billion (OECD, 2009).



Graph 2.1: Worldwide privatization revenues from 1988-2016 (billions of USD)

Source: take a look at ¹

In the privatization barometer report (2016), world privatization proceeds reach the maximum amount ever, USD 319.9 billion in 2015 broking the record registered USD 265.2 billion in 2009. The 2016 privatization was recorded the second-highest of the time amounting to USD 266.4 billion. In terms of stock, the 2013 to 2016 world privatization proceeds were USD 998.8 billion, almost one trillion. China and Britain were at the top, being china collected above half of the world, 54.1% (\$173.2) and 55.6% (\$148.0) in 2015 and 2016 respectively. According to Glen et al (1996), the world's private investment is increasing while the public share is declining simultaneously. In the time of 1990 and 1995, the largest private investment increase was registered by Malawi, Mauritania, Benin, Papua New Guinea, and Bolivia. This shows the situation of poor developing countries also joined and responding to the supply side of the economy. Privatization proceeds exceeded \$1.189 trillion between the times of January 2012 to December 2016 (Megginson, 2017).

¹

Note: 2016 is a preliminary result.

Source: privatization Barometer available at

http://www.privatizationbarometer.com/PUB/NL/5/9/PB_AR2015-2016.pdf

2.5 Privatization Trend in Africa

Developing countries including the Africa privatization program is stimulated by internal politics and external pressure (see Adam et al., 1992; Ramanadhan, 1989; Cook, 1986). In the post-colonial period, most African nations followed the government lead developmental public managed economy. Countries like Ghana followed developmental state economic policies. Even if many suspect developmental state ideology's existences in Africa, there were developmental states in aspiration and economic performances (Mkandawire, 2001). In the 1980s, neoliberal orthodoxy harped on the deleterious effects of state intervention and insisted on the advantages of market-driven development. For Mkandawire the first squint of the Asian experience of growth with the strong state was done by the Berg report that was used as the adjustment document. The World Bank was congenitally tied to the core argument of the Berg report with its faith in the market and a minimalist view of the state. Then after Africa fall on the hands of the westerns and their implementer organizations.

Governments in Africa have not always adopted privatization for the stated reasons. The program has been prompted in many cases by various factors of economic and enabled by the political changes. According to Bhatia et al (1998), although reduction of fiscal deficit is commonly cited objective of privatization in Africa, the selection of enterprises for privatization suggests the primary motivation have been the need for the world bank, IMF and donor financial institutions support and the need to generate proceeds and divest some troubled state enterprises while minimizing the political fallouts. In the 1990s Africa has fallen in position of questioning what to privatize and how to privatize not whether to privatize or not. Despite the myriads of constraints facing Africa governments and implementing agencies, privatization progressively expanded in the region and in the period 1990-1995 state owned enterprises declined by third (Bhatia et al, 1998). In their case studies they found it is corrupted and not transparent with a significant employment reduction in the post privatization period.

The justified reason for privatization varies from country to country despite its controversial and complex most researchers inclined to most African privatization takes place as part the broader adjustment program under the auspices of international development organizations or donors Ghebreyesus and Suliman (2001). The international organizations of the World Bank and IMF are concerned with the necessary macroeconomic stability which entails fiscal discipline and privatization. But the reality in Africa shows that privatization is political driven and not the auspice X-efficiency and economic growth.

Table 2.1: Size and Suspected Motivation of Privatization in Africa, 1995

Country	Size of Public Sector (% of GDP)	Motivation
Angola	64.1	ethnic
Burundi	13.0	ethnic
Cameroon	21.6	ethnic
Central African Republic	26.6	ethnic
Chad	29.4	ethnic
Congo, People' s Republic of the	38.8	n/a
Côte d' Ivoire	24.8	ethnic
Djibouti	42.0	n/a
Ethiopia	27.6	ethnic
Ghana	19.6	ethnic
Liberia	50.5	ethnic
Madagascar	13.3	ethnic
Mozambique	43.4	ethnic
Nigeria	15.8	religious
Rwanda	112.4	ethnic
Somalia	51.3	ethnic
Sudan	25.0	religious
Uganda	15.1	ethnic
Zaire	32.6	ethnic
Zambia	32.6	ethnic
Zimbabwe	45.0	ethnic

Source: Adapted from Suliman and Ghebreyesus (2001)

As can be seen from the above table2.1, the primary motive for privatization in Africa for the sampled 21 countries is ethnic based political motive. From the table Ethiopia has an average 27.6% public size relative to the extreme top of Angola (64.1%) and extreme bottom of Burundi (13%). It is a significant size that can impact the economy.

The Oliver Campbell and Anita Bhatia (1998) privatization analysis in Africa for the World Bank is the biggest and multifaceted in addressing many countries, methods, scopes and performance evaluation. In their analysis, Bhatia and white found major workers layoffs and liquidation as the major privatization method which later over taken by the competitive share sales. Another interesting conclusion made by is the absence of public consensus on the program mainly arises from the non-transparent works of the government and absence grassroots works made on it.

In relative assessment of the program in terms of adherence and success in sub-Saharan Africa, again Bhatia and White (ibid) put Zambia as a good example in its government commitment for the program listing the success factors of;

- Active involvement of the private sector
- Sufficient resource invested in careful program design and preparation
- Full support of privatization by appropriate legislation

→Establishment of a well-financed, legally mandated agency that is free to undertake its mission as a sole privatization institution, with a minimal political interference

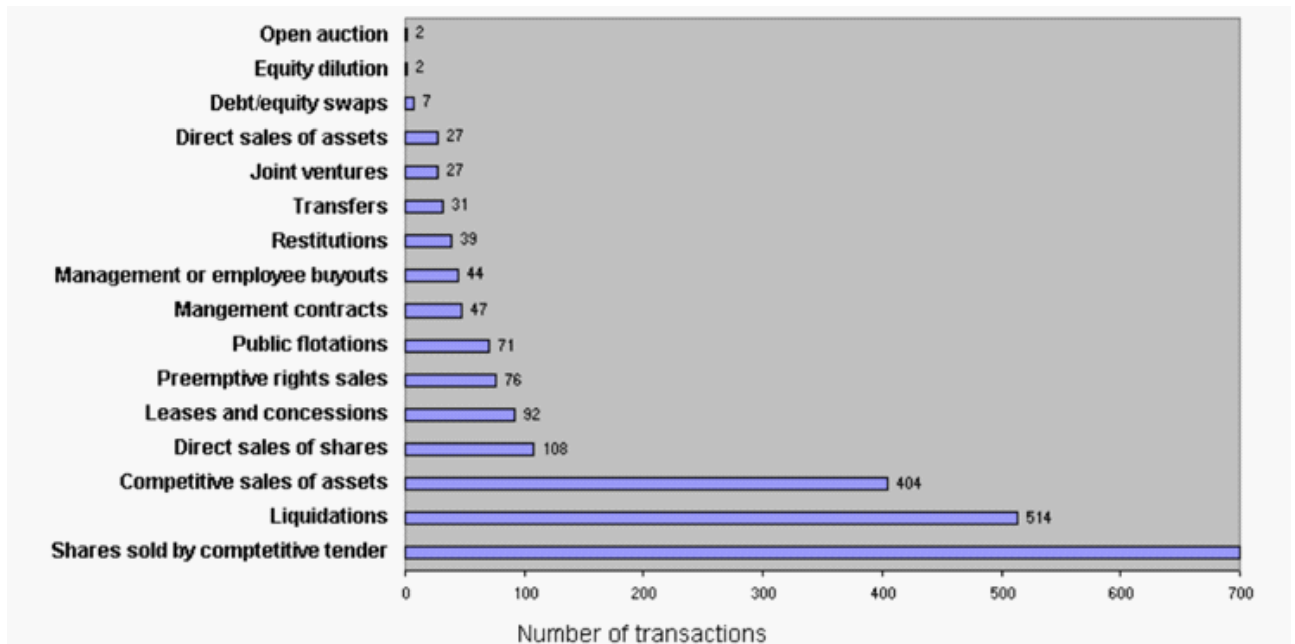
→A full transparent process that has depoliticized the privatization process

→A government and privatization agency that takes decisive action to eliminate the constraints, notably in addressing the weak capital market and the delays in the maneuvers of transferring the companies

→Major efforts to inform the public about the process and to encourage the participation

→Adequate support by the donors

In assessing the methods of privatization in Africa, it has shown fractures. In the starting of privatization, most African countries implemented liquidation, recapitalization and others in noncompetitive ways. Liquidation, asset sale and recapitalization show the weak status of the privatized enterprises by the time. Of course latter the share sales through competitive tender takes place, the most competitive ways of capitalization and voucher-based mass privation was out-of reach or was not among them.



Graph 2.2: Privatization Methods Applied in Africa from 1988-1996

Source: adapted from Makalou

Sub-Saharan Africa implemented privatization in successive waves some started earlier and some others latter (Bennell, 1997). The beginners were the Francophone West African countries of Benin, Guinea, Niger, Senegal, and Togo in the late 1970s and early 1980s, whereas the

second group Francophone and Anglophones of countries was composed of Ghana, Nigeria, Ivory Coast, Mali, Kenya, Malawi, Mozambique, Madagascar, and Uganda, started privatization in the late 1980s. According to Bennell progress was very limited except Nigeria until the 1990s. The program was often influenced by the pressure from the international financial institutions (Nellis, 2012). The last groups are or late starters have shown different political commitments to privatize state-owned enterprises. The first subgroup of countries that show a strong commitment to privatization includes Tanzania, Burkina Faso, and Zambia. And the other sub-groups that shows minimal political commitment to privatization is in Cameroon, Ethiopia, and Sierra Leone.

According to Nellis (2008) privatization in sub-Saharan Africa was very slow and sold about 40% of state-owned enterprises in the period 1990 to 2001. In relative terms, this was very smaller than in Latin American countries. Strong privateers of the time were South Africa, Ghana, Nigeria, Zambia, and Cote d'Ivoire. While the most privatized sectors were food processing, alcoholic beverages, textiles, cement, and other non-metallic products, and metal products. In explaining the slow movement of the program in the 1990s, Bennell 1997, explained by the lack of political commitment and strong opposition from the public sector workers who are going to be touched by the policy, older bureaucrats. For instance, in Cameroon, only five of the thirty SOEs scheduled for privatization were sold by the end of 1995. In other countries such as Nigeria, the privatization program started well but then stalled.

Despite the fact that Nigeria's program had been one of the most successful in SSA in the 1990s, it was suspended in early 1995 in favor of a mass program of "commercialization". In Madagascar, the privatization program was also suspended in mid-1993 due to serious mismanagement and its subsequent unpopularity (Estrin et al 2018). In addition, Bennell (1997) reports that there were nationalist concerns about the possible political and economic consequences of increased foreign ownership as a result of privatization.

However, in the 1990s and later some political loads were lifted from the government's shoulder in terms of ideological changes and the weak financial and operating performances of state-owned enterprises raised the need for privatization in the region. The external pressure from the World Bank and IMF was very significant with the fiscal crisis of the 1990s. This arranged the way for the government to raise its revenue and reduce expenditure by selling enterprises owned. Despite the above explained slow move of privatization in SSA between 1988 and 1999, service and manufacturing accounted for 36% of the total USD 9.8 billion. The infrastructure sector accounted for 28%, energy 17%, primary sector 14% and the financial and others 6% of the total revenues of the region (Estrin and Pelletier, 2018). Then after 2000 to

2008, privatization was very progressive where total proceeds increased to USD 12.654billion.

The above sectoral share also changed in a way that infrastructure gets the first representing 73% of the share of the total deal. The manufacturing and service accounted for only 17% followed by the financial sector 6%, the energy sector decline from 17% to 4% and lastly the primary sector 1%. According to Estrin and Pelletier, the post-2008 periods SSA privatization has shown a slowdown. Even though there is no World Bank privatization data in the post-2008, it seems privatization has declined as seen from the deals and contracts. The exceptions of the period were the Benin privatization of the cotton, the public utility sectors and the majority stake in the cement company were awarded to a strategic private investor in September 2009 and March 2010, respectively. Nigeria was also notable for its sale of 15 electricity-generating and distribution companies in 2013, raising \$2.50 billion (see Megginson 2014). In 2015, after the 2010 failed trail, Chad re-launched 80% of Société des Telecommunications du Tchad (Sotel-Tchad) for sale.

In terms of methodological presenting, Makalou (1999) noted the first listing of BERG (1994) liquidation the dominant privatization method based on the World Bank African development indicators in the 1990s. Despite the various methods of privatization, Makalou presented liquidation the second next to share sales by competitive tender.

2.6 Empirical Literature Survey

In the quest for growth, the capitalist's market lead economic development takes more attention and the ownership-property right theory role for this type of development is at the forefront. In general, privatization is associated with economic liberalization, free trade, competition, and limited government intervention. In order to shed light on the process, motive and benefits of privatization from the empirical studies, let's divide the studies in the west and developing countries group.

Studies on the west countries: The empirical evidence collected so far on the effects of privatization in developed countries is inconclusive like developing countries. Wright et al. (1993) show that in several cases privatization has had a positive impact on firm performance through so-called management buy-out practices. On the other hand, other studies indicate that privatization policies have resulted in the transfer of a large amount of public wealth into private hands. For example, a study by Shaoul (1997) on the privatization of the provision of water shows that contrary to the government's expectations, no efficiency gains were achieved, a percentage of workers actually lost their jobs, consumer prices rose, and the infrastructure

deteriorated. In a study conducted in 1999, Arnold & Cooper report that the UK government only received £ 13.1 million for the sale of a port, which was resold 18 months later for £ 103.7 million. Those who mainly benefited from this undertaking were the managing directors and the banks that financed the buy-out.

Nellis (1999) concludes his overview of privatization in transitional economies by noting that in institutionally weak countries privatization has led to stagnation and the recapitalization of companies, instead of better financial results and increased efficiency. He stresses, however, that renationalization or postponement of further privatization is unlikely to provide any major gain. Governments that botch privatization are equally likely to botch the management of state-owned firms. According to Nellis privatization in Central and Eastern Europe did not always live up to expectations. But no evidence that its alternatives would have brought about better economic outcomes has yet emerged. Frydman et al (1999) analyzed the central European transition economies privatized and state firms' performance. Privatization for outsiders (foreigners) has better performance than the insider in revenue performance but not in cost and overlooking the revenue effect for the outsiders leads to overstatement of the potential employment losses from the post-privatization restructurings.

Empirical studies on developing countries: Privatization as an ownership transfer from the public to the private sector is extensively studied, even though it is inconclusive (Cook and Kirkpatrick, 1995). A study by Abdulkadir (2016) on 142 countries for the period of 1960-2014 in different scenarios, found a positive relationship between privatization and GDP per capita growth. In the study the effect of privatization in the case of developing countries is positive, but in the regional grouping, it varies consistently to the other studies. It is negative for Africa albeit insignificant while the effect of privatization has a slight increase in Latin America and the Caribbean, and Asia and a 3-4 percent increase of GDP per capita in rich countries of Oceania, Europe, and North America. In the volume of the impact, the study found a threshold level, which around the middle-income countries that have high debt and high growth at least then the least developed countries but didn't suffer any conflict. According to the study, the impact is successful in the large privatization in the competitive and financial sectors. In the meantime, success is found larger in the manufacturing and energy sector. Even the effect is larger in the infrastructure area with the larger privatization. Finally, he found a weak relation between privatization and IMF loans.

In another study, Rahbar et al (2012) studied 41 developing countries for the period 2000-2008 and comes in the conclusion that privatization has a different effect across different regions. In the OLS regression controlling other institutional and quality variables found privatization

had not a significant relation with growth in the regions Latin America, Caribbean, sub-Saharan Africa, and the Middle East and North Africa (MENA) region while in the regions South Asia, Asia, and Pacific area, central and western Europe had a significant and positive effect on growth. In addition to the regional difference, they showed the policy's effectiveness dependence on the method of privatization.

Bennet et al (2007) studied 23 transition countries for the period 1990-2003. In the objective of analyzing the effect of the method of privatization on growth, they found only voucher privatization has a statistically significant and positive relationship with growth. The method of privatization's effect on growth is argued in terms of ownership-ability to manage. The capital market development plays a significant role in matching the right entrepreneur to the firm in enabling to bid. They argued in the early stage of transition economies, where capital market development is low, the privatization method plays a significant impact in matching firms with the skills required to run them efficiently. If there is a well developed financial market, entrepreneurs can bid and compete to buy the enterprise or share of the enterprise by borrowing.

Although the theory suggests that privatization leads to the improvement of Multinational Corporations' practices, researchers generally show little interest in finding empirical evidence that supports this assumption. The available evidence does not convincingly show clear improvements in the performance of enterprises as a result of privatization. In Sri Lanka (Wickramasinghe, 1996) privatization did not lead to higher levels of profitability or productivity, and after privatization in Mexico, consumers did not benefit at all (Martin, 1995). Besides, a study by Uddin and Hopper (2003), conducted in 13 privatized firms, shows that returns did not increase, state revenues, as well as employment, decreased. In addition, transparency in external reports was not achieved, and some shareholders, creditors, and tax collecting institutions were affected by wrongful transactions. A study by Boubakri and Cosset (2002) analyze Africa's privatization experience using a sample of 16 African firms divested through public share offering during the period 1989-1996. They document significantly increased capital spending by privatized firms but find only insignificant changes in profitability, efficiency, output, and leverage. This is an interesting result in the case of Africa, which bolds out the failures of the Structural adjustment program, as the study covers the actual implementation time.

Asechemie (1997) argues that concepts such as owner profit or wages are irrelevant in Nigerian society, particularly in the informal sector. This problem is also pointed out by Perera (1989); he indicates that accounting practices in their current form are not suited for LDCs because of the differences in business environments, ownership structures, use of ac-

counting information and attitudes towards disclosure practices, which stem from the colonial era. Therefore, some degree of the reserve concerning the assumptions of the advocates of privatization is justified (Burchell et al., 1980). It can be concluded that the adoption of Western Multinational Corporations techniques by LDCs leads to problems because of the different socio-economic, cultural, and political circumstances (Hopper et al., 2004).

The important question in the impacts of privatization is even if it boosts growth, which type of growth does it have for a country? La Porta and de-Salines (1999) studied Mexican divested firms' and found out-put increased by 50% and employment declined while wage improved for the residing workers. There might be a significant improvement in output, efficiency, profitability, financial and economic performance during post-privatization at the firm level. But this is by overriding social welfare and adversely affecting the distribution of income. Thus, in a country like Ethiopia where more than 2million new labor joined the labor market annually and overstuffed public enterprises are found, privatization would and could result in unemployment and adverse income distribution. In empirical study Gebeyehu (2000) found a 12 percent decrease in employment in Ethiopia privatized firms.

Although the privatization effect on public finance in the short run is increasing the liquidity of the government, its long-run effect is ambiguous. Privatization may be undertaken as a response to fiscal crises (Yarrow, 1999: Dos-Santos, 2007). Privatization generates lump-sum revenues and reduces the government burden of subsidizing lose making enterprises and further investments on the privatized firms. Thus, in the analysis of the long-run net government wealth effect of privatization in Brazil; Dos-Santos, (2007) found that net Brazilian government wealth reduced in the long-run due to the insufficient competition in bidding and cost incurred in the privatization process. But this will be recovered if the future stream of benefits the private sector generate substantial positive difference than the government would have obtained from the privatized firms. An empirical finding, Santos proofed that Brazilian average privatized firms' financial performance hasn't improved and the government expected future tax income hadn't improved. The lack of performance improvement in the privatized firms is explained by the factors of remain dependent on the state for investment financing, some firms are highly regulated where prices are set by the government and the possibility of acquisitions and oligopolistic power formation. Finally concluded, that privatization policy represented a net loss to the Brazilian government, and therefore to the taxpayers in general since they are the ultimate owners of the state-owned enterprises. For Santos designing a privatization program to promote competition and maximize efficiency may reduce the above problems.

Despite the dozens of studies that are on the shelf, the determinants of privatization are still

debating researchers and policymakers owing to the difference in local conditions and desires for privatization. The developing countries' determinant factors are quite different from developed countries. In this respect, Breen and Doyle (2013) studied taking 77 developing countries for the period 1988-1999 and 41 developing countries for 2000-2008. The study extensively analyzed the determinants difference even in a single country on the initial decision to privatize or not and then the extent and scope of the policy implementation. They used the panel cross-section probit model specification with a completely different measure of the privatization variable. The privatization variable is used as a percentage of labor and value-added. In their two stages analysis, Doyle and Breen found the determinants of privatization for the first time are exogenously driven by the degree of capital mobility, the desire to emulate privatizing neighbor, and the IMF conditionality. Then once privatization started, what to privatize and how much to privatize is shaped by the domestic economic and political factors. An interesting result in this study is that countries that participate in international trade more, have less desire to privatize than the others, but ones started that they implemented extensively. They argued that countries delay starting privatization due to the firms' desire for strong protection and regulation from the embarked competition.

In a study by Cook and Uchida (2003) on 63, developing countries in 1985-1997 using extreme bound analysis (EBA) found a negative and statistically significant relationship between economic growth and privatization. This result is different from the results of the previous studies by plane (1997), Barnett et al (2000). It is argued that the methodological and sample difference creates this result owing to the outlier and other robustness checks are better in this study. This study is a re-affirmation for the previous study of their own, Cook and Uchida (2001). Another study by Filipovic (2005) in a relatively similar model specification for the whole developing countries that have data on privatization by the time of 1990-1999 re-affirmed the negative effect of privation on developing countries' growth despite the policy has a strong correlation with other economic variables used in the study. Thus, the researcher concluded that privatization is sensitive to other economic reforms and incentives for the potential positive impact on economic growth. On the other group, privatization is neutral for growth while a competitive regulatory environment has a positive effect on growth (Moshiri and Abdou, 2009). This supports the hypothesis that not privatization alone but competition with regulatory system boosts growth.

The social welfare of a policy change comes from the consumers, workers, tax-payers, and any stakeholders. In the policy change of privatization, it includes suppliers and competitive in the market. Like the other effects, the welfare effects of privatization are inconclusive resembling

to the negative effect.

A study by Bonnet et al (2009) using the 1995-2005 period Latinobarometro survey data for 17 Latin American countries in the analysis of the determinants of the public discontent about privatization, comes in two-fold relative and absolute welfare effects. They indicated the relative discontent is from the unequal distribution of income of the efficiency gain among the population, whereas the absolute discontent or dissatisfaction arises from the public sector employees and unemployed. Individual expectations and beliefs have an insurgent effect on the dissatisfaction of the public. According to the study, beliefs affect the publics' decision about the satisfaction of privatization policy in two channels. First, in the information channel, Individuals forming pessimistic evaluations of the economic situation or the quality of trust in their society, infer from there that policy choices may have been misguided or that they may reflect opportunistic behavior by policymakers. Second, opinions on privatizations reflect different expectations with the outcome of this policy or with the way it is conducted. This explains for example that individuals who place themselves more on the right economic ideology of the political spectrum are more dissatisfied than those on the left.

In the study of the policy privatization, Benerjee et al (2002) analyzed thirty-five low-income and middle-income developing countries in terms of time, pace, and intensity independently. In the analysis of the decision to privatize, calibrated by the net political benefit; proxied by an array of macroeconomic, political and institutional variables, found different result although the political benefit turns out to explain the three variables. Its effect varies in each variable. According to the study, the decision to begin to privatize (time) is fundamentally different from the choice to implement select particular units to privatize (pace) and begin to sell off assets (intensity). In addition, the study concluded that privatization is not the best-chosen policy with long-term goals; rather it is a crises-driven, last-ditch effort to turn the economy around the normal. Failure of the privatization policy is explained by the conflicting power use of large public sectors for the timing of the policy. For this, they found two institutions that have a significant effect are the foreign aid regime and the development of the property right system.

It is an important issue that from where did the government starts privatization and at a point in time which enterprises are prioritized for privatization. According to Gupta et al (2004) privatization can't be undertaken once due to several reasons. Amongst it, the government may prioritize for privatization to reduce congestion and transaction cost besides the information revealing cost to the potential investors. The government may prioritize to avoid any political opposition for dramatic reforms and lastly, to reduce any welfare losses concerning the reform such as wage cut or employment losses. Gupta et al (2004) used the Czech Republic firm data to

investigate the strategic move of the state in prioritizing. The result supported the hypothesis that the government starts privatization from the most profitable enterprises and that has large market shares for its revenue and public goodwill maximization.

Shukurove et al (2016) studied the transition period effects of Uzbekistan privatization policy on economic growth for the period 1994-2014, using time series analysis, and comes privatization has a positive and significant effect on the growth of the nation. This is consistent with other single-country studies of Desalegn et al (2018). Desalegn and Reddy studied the growth effects of privatization for Ethiopia using the semi-annual data of 1994-2016, in a time series analysis. In another single country study on the macroeconomic impacts of privatization Ozata (2014) used the Turkey data for the period 1986-2012 and analyzed the growth effect of privatization in a time series methodology. The error correction model result posits a negative statistically significant result of privatization on economic growth. In general, both cross-country and single-country studies reveal inconclusive impacts of privatization on economic growth mostly due to the data and methodological differences in addition to different country-specific factors.

Chapter 3

Descriptive Analysis and privatization Trend of Ethiopia

After a short brief of the three regimes of Ethiopia is presented, the descriptive analysis of the interest variables is going to be presented. In a time series analysis of this study, the trend analysis of the main variables of interest will be presented aiming the following objectives. First, the graphical presentation has significant importance in portraying the information about the movement of economic growth and specified exogenous variables. Second, trend analysis is the easiest way in presenting the dynamic movement of the variables. Lastly, this being part of data exploration, has the potential to inform the appropriate method of analysis for the econometric model of part five.

3.1 The Imperial and Derg Regime

In this sub-section, the major macroeconomic policy, trend, and circumstances of the most recent three governments are presented putting more focus on the Derg socialist-nationalization program and the follower EPRDF that wrenched power from the former. In the long book chapters of Ethiopian history, agriculture covers the longest part. The first national economic plan for development was undertaken by the imperial regime of the 1950s. Then after the regime made two consecutive five-year plans, a total of three, and wrapping up the preparation of the fourth five-year plan when the military regime comes and overthrow it.

The overall economic evaluations, done by Chole and Manyazewal, (n.d); Geda (2001); Geda and Degefe, (2005), have found a positive and good result even though it was deteriorating during the last time of the regime. According to Geda and Degefe, the imperial regime was the time an attempt to modernize the country was made in such a way that expanding education,

health facilities, infrastructure, the introduction of the constitution, the mid-term national plans to list some. With this, the imperial regime pursued a market lead economy and accomplished a positive and respectable growth. In the last time of the regime (i.e. 1960-1974) Ethiopia's macroeconomic performance was 4 and 1.5 percent economic growth and per capita income growth respectively.

Despite the archaic misery system of the economy in the agriculture sector in the period of 1967/8-1971/2, agriculture accounts for over 57% of GDP and the most dominant source of employment and foreign exchange (Chole and Manyazewal, n.d). Even though the economy shows a deceleration in economic performance at the beginning of the 1970s, in the period 1967/68-1971/72, export of goods and non-factor services grew by an average rate of 4.7% and 4.6%, 33.2% and 26.7% in the period 1971/72, 1972/73, 1973/74 respectively. The import of goods and non-factor services grew by an average of 3.4 percent in the period 1967/68-1971/2. The economy during that time has shown significant growth in saving, low inflation, and outstanding debt repaying which in turn low fiscal deficit and capital expenditure, but a decline of gross fixed capital formation to list some. In conclusion, Chole and Manyazewal said, Ethiopia in the eve of the 1974 revolution has had a good and respectable economic and per capita growth with low inflation, a comfortable balance of payment and a growing domestic saving ratio, but a declining gross fixed capital formation.

The structural problem of the economy that is the serfdom of the poor in the rural part of the country coupled with the government's alienation fastened the fall of the regime (Clapham, 1988; cited in Geda and Degefe, 2005). The immediate cause for the fall of the regime for Geda and Degefe is the famine in northern Ethiopia, which the government attempted to hide, the riots of taxi drivers following the 1973 oil price crisis, and the opposition of the educated elites against the educational curriculum modification. The already eroded social and political base of the government and the above mentioned immediate causes a mass movement culminate the imperial regime's power by the Provisional Military Administrative Council (PMAC)(Chole and Manyazewal, n.d).

The immediate task of the military regime did after toppled the imperial regime was mobilizing the people for the catch-all motto of "Ethiopia Tikdem". In 1974 it declared socialism as the lead guide and the motto defines Ethiopia Tikdem" meant equality, self-reliance, the dignity of labor, the supremacy of the common good, and the indivisibility of Ethiopia's unity (PMGE 1974; cited in Chole and Manyazewal,n.d). The survival of the regime was hanging on the position that it would answer the land question (Geda and Degefe, 2005). In its socialism declaration, the regime tried to delineate and indicate the economic activities and sectors where

the state, private sector, and foreign capitals invest and operate. In doing this Derg nationalized all banks, insurance companies, and industrial and commercial firms and the land reform by the creation of the peasants Association (PA). The urban land and extra house owned by the private was nationalized at the end of 1975.

In late 1976, the national democratic revolution (NDR) in its advancement on the former for socialism declaring Marxism-Leninism and in the 1987 workers party of Ethiopia (WPE) used as the details for the ten-year plan of the period 1983/4-1993/4. The plan is similar to the EPRDF ADLI plan in some sort of objectives and targets. Expecting to entail a considerable structural shift in the economy, the plan set the major goals of an average annual growth rate of 6.5% in real GDP and at the same time of 4.3%, 10.8%, and 6.9% an average annual increase in the agriculture, industry and service sector. In its grassroots ideological and pragmatic socialist program, the Derg regime discouraged the private sector prohibiting participation and putting different hurdles in the business environment. Having this and the like the Ethiopian economic performance was the most the worst of the others, in which Chole and Manyazewal reported the growth of the time (1974-1990) was 1.9 which is much lower than the last time of the imperial era and expressed as the lost years in the history of the country.

The overall period of economic performance is uneven mainly with the change in weather-shortage of rainfall and conflicts with neighboring country-Somalia and at home. The period 1974-1978 was the time of internal conflict and war with Somalia which drastically harmed the growth of the country. The next period of 1979-1983 was the recovery from through the ‘Zemecha’ program by the all-out annual campaign for hastening growth, which registered a respectable rate of 4.2%. This was followed by the 1984/85 catastrophic droughts and famine that suddenly starved over 8 million people. The following two years were the recovery time again due to sufficient rain and relative peace, which didn’t stay long. But in the period 1988-1990, the rapidly expanded war and conflict devastated the growth of the economy with other factors leading to the beginning of the end of the regime. From the above general macroeconomic programs of the country and its performance presentation, we have to learn the basic factors responsible for the uneven growth performance and economic activities of the country. First, agriculture, which accounts for above half of the national population, employment, share of GDP, and foreign exchange is the most dominant source and determinant of growth of the country. Second, the political process intervenes in the economy negatively. The scramble for resources and power devastates the economy.

The Derg regimes 17 years represented the lost year in the economic performance of the Ethiopian history for most economists who evaluated it. Despite the macroeconomic perfor-

mance in growth; saving and investment due to the raising of government consumption expenditure for military with the counter saving declines, debt accumulation, and loss of interest of international donors to lend for worsened any reforms result.

According to Chole and Manyazewal in that period government deficit financed by external sources accounts for 59 percent and reached a peak of 86 percent in 1987/88 until it declines to 35 percent in 1989/90 due to the drying up of the external sources. This was followed by the deteriorated export performance and increasing money supply added up to become inflationary. These factors with others drawn down the foreign currency reserve and make empty the treasury. Another important factor that should be included in this analysis is the balance of payment. The balance of payment showed a deteriorating trend following the sluggish export and increasing import. The only positive current account section in time was the service part due to Ethiopian Airlines, which is our proud of any time and place but proposed to be privatized now.

The aforementioned factors of the internal and external coping with the decline of socialism in west Europe and Russia federation forced the government to take series reform not only ideological but also pragmatic changes. That is why the 1988 mixed economy system comes to the front. In this reform, the government accredited the role of the market in growth and development through lifting the previous restrictions and providing incentives in tax exemption and creating a competitive environment for the domestic private and foreigners. But still, the government hand in the economy continued substantial.

The mixed economic system failed to ripe the targeted grapes mainly due to the lost socio-political base and lack of confidence by the private in the business environment. The uncertain political and legal environment discouraged foreign investors even after opening and some incentives are provided. The international donors' sources of the fund still out-off reach from the reluctance of the donors. Lastly, the resource continuously mobilized for war or military purposes ignoring development agendas aside. These hasten the fail of the military government for the upcoming transitional government and later EPRDF which goes back to the marketed informed system.

3.2 The Post-Derg of Ethiopia

The primary activity the EPRDF government did, counter to the Derg did, was de-nationalization of the nationalized enterprises of the Derg government. Ethiopia in the deceleration of economic performance falls on the hand of the transitional government, one of the opposing force, and the international organizations. Promising the issue of poverty reduction by rebuilding of infrastructure, stabilizing the economy and reforming institutions, the World Bank's policy articulated in successive country strategy papers (CSPs). With the cessation of hostilities in 1991 and the assumption of power by a new Government, the Bank approved in 1992 the Economic Recovery and Reconstruction Programme (ERRP) as its first multi-sector operation in the country (ADB, 2008). Since then the long hand of the Breton woods institutions resides in the country. The EPRDF government designed and implemented different economic policies, strategy papers, and programs that all done with the international financial institutions in different manners.

The economic recovery and reconstruction program, the national interim-poverty reduction strategy paper (I-PREP), sustainable development and poverty reduction strategy (SDPRP), and plan for sustainable development to end poverty (PASDEP) all nested in the national plan of agricultural development lead industrialization (ADLI). The two structural adjustment programs (SAP I, II) supposed by the World Bank with the aforementioned programs supposing rehabilitation, reconstruction of infrastructure devastated by the civil war. The bank's primary objective stated in the program was reducing poverty by fostering growth through capacity building, education, health, food security, and stable macroeconomy to mention some.

According to Geda (2001), there were at least three main reasons for the political ideology shift from socialism to a market-oriented economy by the EPRDF government, although it was informed by socialism before it comes to power. First, the collapse of socialism internationally mainly in Russia, and it had to confront the domestic dissent towards socialism by bringing antithesis of socialism to the front forced to accept than make any choice. Second the deep-rooted political dichotomy in the elites and the government. While the ruling EPRDF takes the position of "self-determination including cessation" for regions organized along with language and cultural lines, many political groups, including the majority of the inherited bureaucracy, oppose this framework. In this political landscape, it was rational for the EPRDF to accept the reform not only to get external endorsements but also to use macro policy instruments (such as expenditure reduction) to fight the hostile bureaucracy. The third reason was Decentralization, although it is the Briton woods recommendation for Ethiopia as one of the liberalization schemes, it rooted in the EPRDF's ideological rule.

Despite the foregoing reforms and international exposures, the country faces challenging problems of debt stress, low saving, unemployment, weak financial intermediation, and lack of competition that can hasten growth for poverty reduction plans. Growth in the post-Derg period is good in terms of real total and per capita GDP (Geda, 2001). Despite many structural problems are there on the ground, the positive performance of the economy is not covered from the eyes of anyone. But, this does not mean that there was no problem. The debt burden of the economy has ever increased. The World Bank estimates that Ethiopia relies on development assistance to the tune of 40 percent of its public sector spending. The high degree of dependence makes domestic investment highly dependent on foreign savings thereby creating policymaking uncertainty in the country. This creates a significant shortfall that dependence on foreign resource flow could put growth prospects at risk. In 2000/01 the country falls in a high debt burden of estimated at about USD 5,358 million, which is at about 89% of the country's GDP and external debt ratio of 23% (ADB, 2008).

Another area of concern central to explaining the reforms and growth of the country is the competition performance. De-nationalization persuaded by the government forced by the Breton Woods institutions for the country failed in producing the targeted goals due to many factors and especially lack of competition in the country. The private sector in the country can be described as a duopoly market dominated by the two conglomerates of the ruling party parastatals and the family business (Wedajo nd Senebet, 2017). The economy remains dependent on rain-fed agriculture, which's growth co-moves with agricultural production, and the pace of privatization is slow with some monopolies to exist in the economy in the form of party-affiliated companies, which didn't like a level field playing with private sectors (ADB, 2008).

3.3 Privatization of State-Owned Enterprises in Ethiopia

The Ethiopian government in the 1990s begins reforming the socio-economic environment of the former socialism oriented to a more liberal and market informed system. The transitional government (TG) who took power from the Derg, prepared three-year policy framework and agreed with IMF and World Bank in October 1992. The policy framework in revitalizing the economy informed towards the creation of more market and liberal economy. The reform supplemented by the forthcoming structural adjustment programs of the bank. The banks unreserved admire for liberalization with the countries deceleration in economic performances and the problems of weak SOEs performance, macroeconomic instability, increasing budget deficits, alarming high

external debt and the stable poverty growth, call for unprepared privatization of state-owned enterprises in the beginning of 1990s.

The Ethiopian Privatization Agency (EPA) was established in February 1994 by the proclamation no. 87/1994 in accordance with article 9(d) of the transitional government charter. Accountable to the prime minister's office, the agency takes the whole task of privatization. In consecutive amendments, the proclamation added more power and duties to administer, employ consultants, investigate and decide on claims concerning property rights. But the power to determine the enterprises to be privatized reserved for the government. The proclamation no. 116/1998 puts clear objectives to be achieved by the privatization program. This includes;

→To generate revenue required for financing development activities undertaken by the government

→To change the role and participation of the government in the economy to enable it to exert more effort in activities requires its attention and;

→To promote the country's economic development by encouraging the expansion of the private sector

The issues of determining the modalities of privatization, mode of currency payment, evaluation of asset and its depreciation for future tax, continuity of employees in the enterprise and social security, the transfer rights and obligations of enterprises, and post-privatization monitoring are given to the agency in the proclamation no 116/1998.

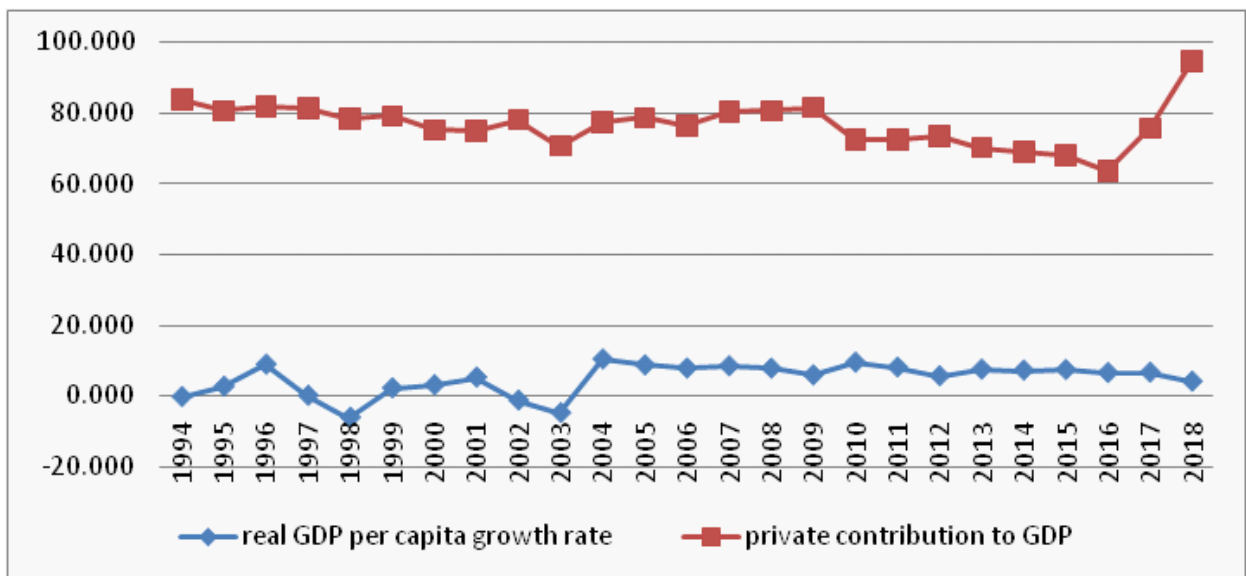
3.4 Descriptive Analysis

3.4.1 Private Sector Development in Ethiopia

The private sector started in Ethiopia during Emperor Menelik II with the acquisition of land (see Deneke, 2001). According to Deneke this private property in the form of land acquisition was by scrambling in waging unsettled inter-war and foreign aggression. This private sector development started during Emperor Haile Sellassie's period again in the form of farm commercial and forward linkage agro-processing. Small industries were owned by the private owners and the constitution supported private property possession and development. Following the overthrow of the Derg socialist regime in 1991, the transitional government of Ethiopia announced a free-market economy. As discussed above, even though the Derg regime reduced the private sector through nationalizing and restricting the private participation, which highly reduced the private sector share in the economy, the transitional government restored the free market economy system. The Derg regime abolished/reduced its restriction in the private sector in the last

time mixed economy announcements.

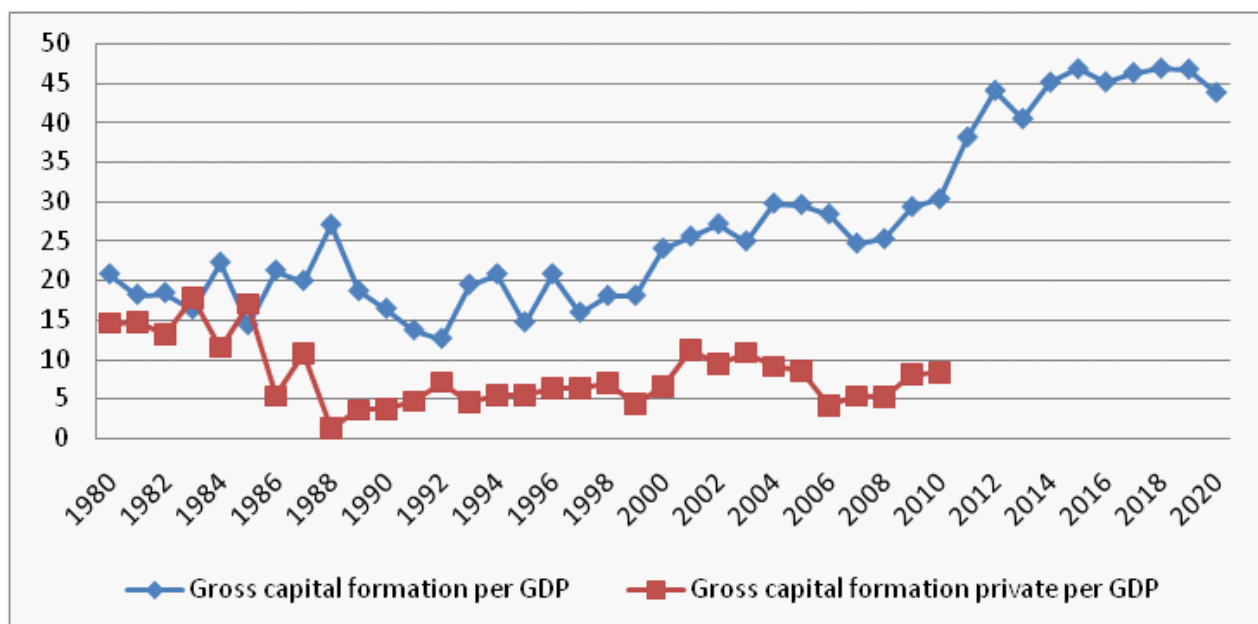
Promotion of mixed economy in private, public and cooperatives operation side by side in a competitive manner, elimination of the restriction in capital ceiling and areas of operation of private enterprises, restructuring of public enterprises towards competition and profitability, the abolition of agriculture corporation quotas, allowing of inter-regional grain movement, and promotion of foreign investments to list some. The transitional government's announcement of a free market economy increased the privileged private investors and the share of the private. But, at this time not only the private the government position in the economy is also high in relative to the private sector.



Graph 3.1: Real GDP per capita Growth and Private Contribution to GDP, 1994-2018

Source: Own graphics

As shown in graph3.1 above, the private sector contribution to national production has almost stable throughout the period. Private sector expenditure as a measure of private sector share of the national income from the national income identity is used. The share has a declining trend in relative terms. Although the time 1991 and after is credit for privatization and deregulation of the Derg socialist system in the process of creating the western capitalist system in Ethiopia. But as shown in the graph, the process has not shown a significant and rapid improvement in the creation and strengthening of the private sector. The share stay relatively stable until 2009 which the lowest of the study period and then rapidly and progressively increased to reach the highest ever of the study period in 2018



Graph3.2: Comparison of Private share in gross fixed capital formation per GDP to the Gross national, 1980-2019

Source: own graphics

As shown in graph3.2 above, the trend of the fixed capital formation shows divergent trend between the gross capital formations to GDP ratio with private capital formation to GDP ratio, in which the latter showed declining up 2010, the time I got data. Ethiopia has shown significant growth in the industry sector, especially in the construction sector that accounts for about 60% of the growth of the sector. Despite this, the private sector share in the period 1980-2010 shows a diminishing trend. As shown from the graph, another interesting point found is the rhythmic and co-moving of the total with the private sector share up to 2002/3 and great divergence, being the gross increase and private decline.

3.4.2 Debt and Economic Growth in Ethiopia

The issue of the debt-growth relationship is not answered yet. Debt creates tremendous investment capacity, especially for developing countries. But it is conditional on the home economic performance and the level of debt that that country has at that point in time. That is the debt overhang problem comes with this. According to Krugman (1998) countries reach the current situation with a stock of “inherited” debt, which they can’t pay without new borrowing. With this most developing countries are in debt overhang problems. By the term debt overhang mean the presence of an inherited debt sufficiently large enough that the creditors expect they will not be repaid. In his study, Krugman found that debt distorts the economic incentives in a way

that, even if the economy performs well, the benefits of good performance by large goes to the creditors and not reside for the domestic.

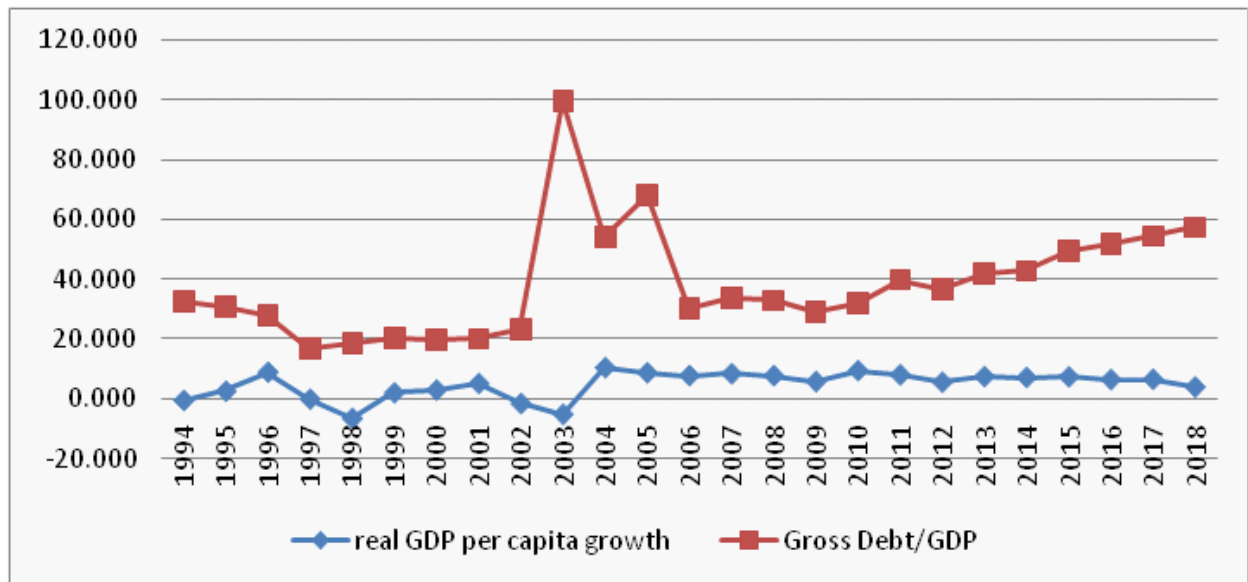
Geda (2001) analyzed the debt problem of Africa and did the HIPIC initiative help to write off debt from Africa? He answered NO! Despite the existence of many factors for the debt problem of the region, he concluded that the main problem emerges from the trade problem. Thus, the long-run solution supposed for is solving trade and trade-related structural problems of the region. The international development association and IMF debt analysis of (2018) showed that Ethiopia is continuing at high risk of external debt distress and overall risk of debt distress. The empirical results of debt in Ethiopia are divergent. But, most agrees on the debt has a positive relation with growth in the short-run but not in the long-run representing debt overhang problem. Ethiopia's debt is increasing through time and it is becoming the countries growth threat.

The total external debt stock is direct government fixed-term contractual obligations to others outstanding at a particular date . This is the debt that is sourced from nonresidents and paid with foreign currency. The net effect of external debt on economic growth depends on the sector or budget type allocated. External debt may cause private investment crowd-out if it is used as the source for government expenditure. But it will boost economic growth if it is allocated for the targeted development investment like infrastructure.

The effect of external debt on economic growth is inconclusive. Despite it creates capacity for the common problem of the developing countries- fiscal gap, external debt may distress the domestic investment by reducing disposable income share for saving, by the increased taxes for the debt service. When the government borrows from abroad, he is going to pay by increasing taxes. It is contrary to the tax to debt financing equivalence of the Ricardian equivalence theory. The Ricardian equivalence theory takes debt financing as an equivalent and similar to tax in a way that, when the government borrows, he is going to increase tax to service the debt. And the households are rational to know that for rebalancing their consumption for the tax increase.

Diamond (1965) looks at the long-run debt effect on growth in two folds, in which both arising from the tax increases to finance the debt interest payment. First, the tax reduces the available lifetime consumption of the individual taxpayer. As consumption is from disposable income, and disposable income is after-tax, consumption declines. Second, the tax reduces saving by the declined disposable income and therefore the capital stock. Internal debt has the above effects and an additional effect of further reducing the capital stock by the substitution of the government debt for the physical capital in the individual portfolios. Therefore the effect

of debt in the ever-increasing stock of Ethiopian debt is difficult to predict.



Graph 3.3: Real GDP per capita growth and Gross Debt to GDP Ratio, 1994-2018

Source: own computation from World Bank data base

As shown from graph3.3 above, the trend of real GDP per capita growth has an irregular trend until 2004 and becomes more stable after 2004. The transition period conflicts and war with the neighboring country Eritrea with vagaries of the weather of the country are the responsible factors of the growth irregularity in the 1990s. The accumulated weak economic performance of the Derg regime is also part of it. But after 2004 for growth it is more or less stable due to the relative weather improvements (i.e. adequate rainfall) and good agricultural performance. The irregular periods of growth of 1994-2003, grew at an average rate of 1.844, while in the relative stable periods of 2004-2018 its growth at an average rate of 7.43, with all period's growth is positive. The formers irregularity and weak growth further explained by the unsuccessful SAP programs of the Breton wood's program. From the same graph, the trend of general government debt to GDP ratio has been in an increasing trend.

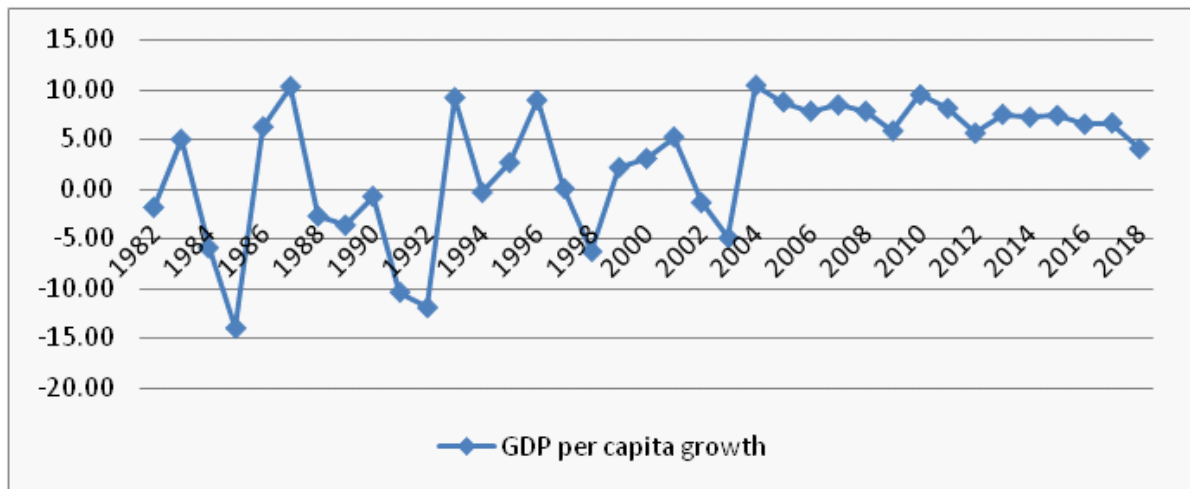
The general government debt to GDP ratio shows a decline from 33% in 1994 to 17% in 1997 and sprawls back after 1997 until reaches the highest 99.5 in 2003 and 68 in 2005. Then it reached 30.5 in 2006 and 29.2 in 2009 the lowest whereas then after it increased almost linearly up to it 57.4 in 2018. Here, we can conclude that, even though there is a positive real GDP per capita growth, the growth rate of general government debt to GDP ratio is faster than real GDP per capita. Therefore, debt may have a short-run positive effect on growth but not in the long term, which is going to be proofed in the econometrics part.

3.4.3 Privatization and Economic Growth in Ethiopia

The growth of Ethiopia has an irregular trend. It is cyclical mainly with the weather change, political atmosphere (i.e. political ideology and the recurrent war and conflict), and external crisis. According to Weeks et al (2001), during the last imperial regime of 1960-1974, real GDP and per capita growth were 4% and 1.5% respectively. This growth experience reversed by the 1974 revolution to 2.3 % and -0.4 in the period 1974-1990 respectively. Growth during 1990/1-1999/0 of the EPRDF government reversed and registered about 3.7% and 0.7% of real GDP and per capita growth respectively. They explained this erratic increase by agricultural performance due to favorable weather conditions. Excluding the worst seasons of 1990-2, they found a very respectable growth of 5.6% and 2.6% respectively.

Gross Privatization Proceeds to GDP ratio: privatization is undertaken sporadically (Plane, 1997; Cook and Uchida, 2003). The gross privatization proceeds as the measure of privatization policy have been used in many studies. Privatization by introducing competition through economic liberalization, exposing public enterprises to market discipline, developing capital markets, and attracting national and foreign investors (Megginson et al., 1994) contribute to economic growth. By achieving these goals government money, otherwise spent on subsidies, will be saved and political and social stability will be achieved through a more balanced allocation of resources. In addition to this, if the government uses the money for the targeted development activities, it stimulates growth by the crowd in effect. On the other side, privatization (domestic) harms private investment in the short-run although the wealth of the private increases. Immediately to the privatization, the wealth of the government decrease and the private purchaser increases. The income effect is the reverse.

The private income increases after the privatized firms start work and generate income. Here our concern the government side that the future income streams has gone. But in this study, the main argument is that privatization hurts growth in the way that Mackenzie (1998) argued. In Ethiopia privatization reduced employment by 12% in privatized firms (Gebeyehu, 2000), production in the privatized firms declined by 14.21% in the period 1995-2004 (Selvam, 2007). Senbet and Wedajo (2017) argued privatization benefited only the existing monopoly and paralyzes competition in the country. Privatization for developing countries is squashed by the westerns and IFIs in a ghosted argument of reducing the non-existing government power. In line with this, it is expected privatization hurts or has no any relation with growth in Ethiopia.



Graph 3.4: Real GDP per capita annual growth rate, 1982-2018

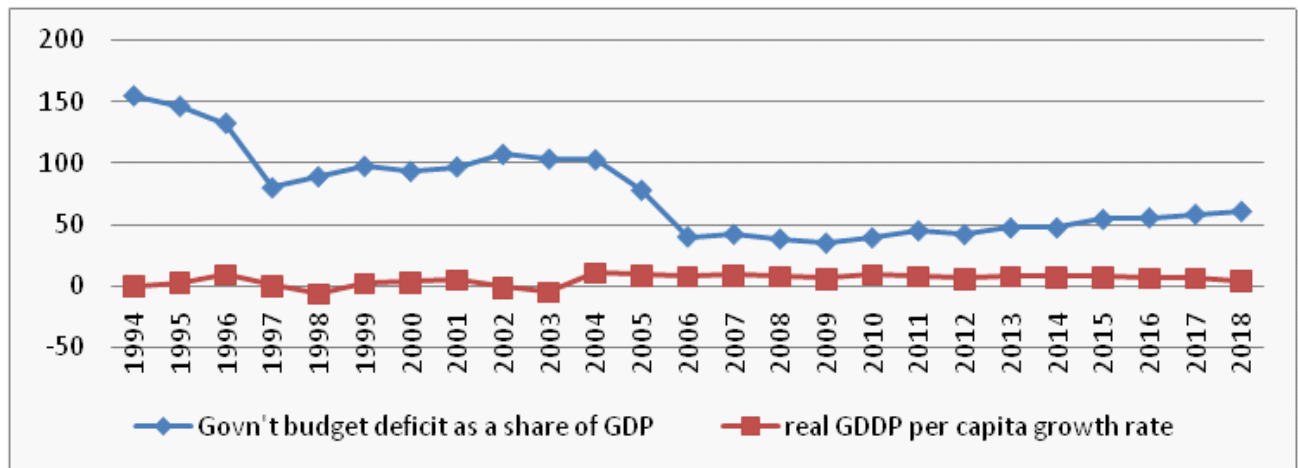
Source: Own graphics

As shown from the graph 3.4, above, economic growth of Ethiopia is more unstable up to 2004 and becomes more stable after this time. The worst growth registered in 1984/5 due to the period's drought and agricultural production decline. According to Geda (2001), growth and agricultural production have a rhythmic and co-movement due to the extreme dependence of the Ethiopian economy on the rain-fed agricultural production. This erratic decline continued in the next periods of 1991/2, 1994/5, 1997/8, and 2003. The next lowest growth registered 1992 about -11.89% and in 1998 about -6.25%. (See graph 3.4). The possible reasons for such erratic declines are the 1991 civil war and drought and again drought for the 1997/8. On the other hand a good outturn in rainfall in 1987/8, 1993, 1996 and 2004 bumper the harvest and economic growth by 6.23, 10.28, 9.17, 8.92 and 10.41 respectively.

3.4.4 Government Budget Deficit and Economic Growth

Government budget balance is the difference between government revenue and government expenditure, which has an immense economic implication and mainly with the debt burden of a nation. Despite there is an inconclusive debate on the definition of government, the standard economics takes tax as the main source of revenue. The service charges, returns from government investments, and external debt sources are part of the revenues used to narrow the deficit gap. On the other side, the government has expenditures for recurrent and capital expenditures. The core point is how large the gap is and how did government finance this gap. The level of the gap, how financed, and or what the government response is for the problem (apparently not by itself a problem). When there is high government expenditure, it means

more investments, and unless crowd out, more investment and return with high employment. This paves the way for growth despite many argue public investments are not commercial or with high returns.



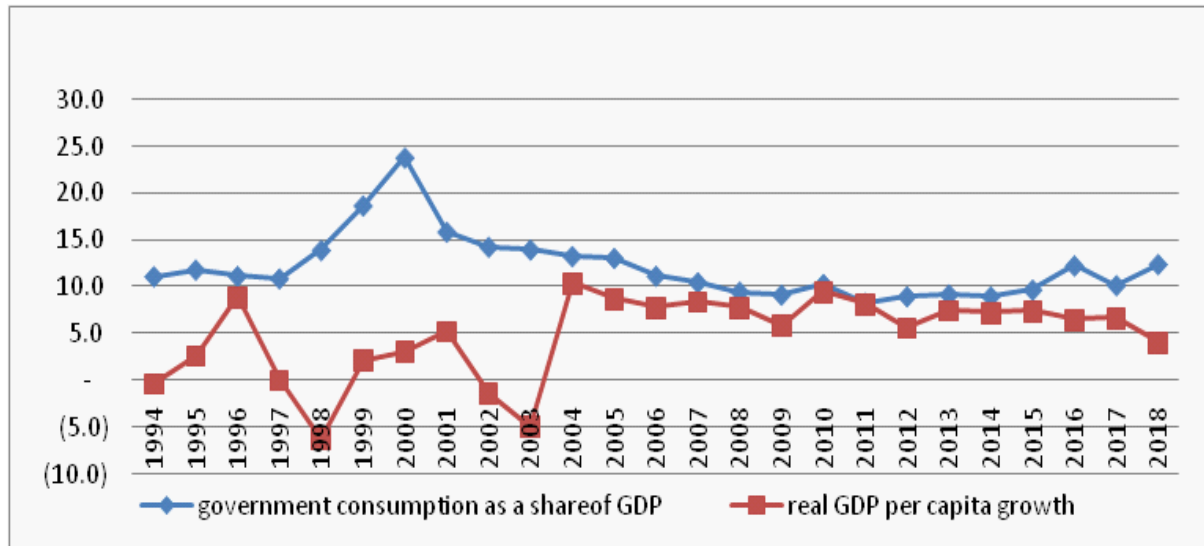
Graph 3.5: Government Budget Deficit and Real GDP per Capita Growth, 1994-2018

Sorce Own graphics

The level of government budget gap by itself shows only the extent of how far is expenditure from revenues. As shown in graph3.5 above, government budget balance has shown a declining trend in the study period till 2006. Starting the study period of 1994 it sharply declined from 155.2 to 80.3 in 1997. Then after it sharply increased to reach the ever maximum of the study period over 107 in 2002 and stay almost stable until progressively decline again in 2004. In the period 2006 and 2012, it was at an average of 40.41 percent. After the 2008/9 world crises, the deficit has been again sharply increasing. The budget balance in 2018 is about 61 percent of gross domestic product.

3.4.5 Government Consumption and Economic Growth

Government consumption expenditure has a significant share in the national income or gross domestic product. Privatization in particular and the Washington consensus, in general, sets the fiscal discipline i.e. reducing the government expenditure. But in practical as shown in the figure its trend has shown increasing or more or less stable trend.



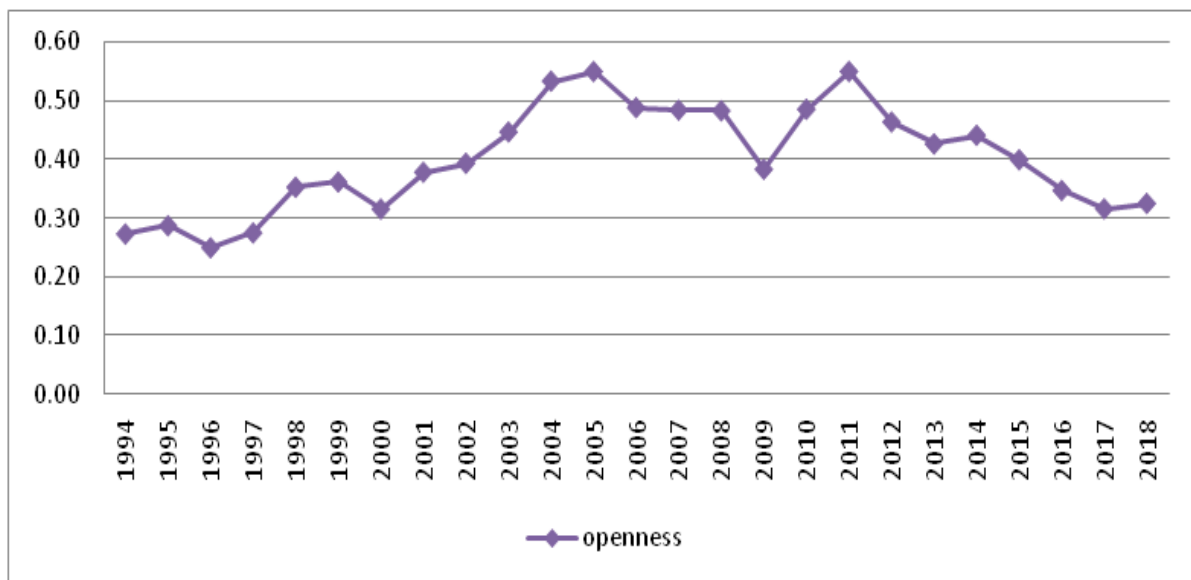
Graph 3.6: Real GDP per capita Growth and Government Consumption, 1994-2018

Source: Own graphics

As shown in graph 3.6 above, government consumption expenditure has an almost stable trend relative to others. It falls around 10 to 15 % of the gross product of the country. Another important point from the graph is government consumption follows a similar trend of real GDP growth. The highest of the period is in 2000 about 23.8% of GDP which is also the highest of the study periods average of 12.12 percent. The most probable cause of this should be the 1999/00 Ethiopia-Eritrean war.

3.4.6 Trade Openness and Economic Growth

The level of competitiveness of a nation in the international environment, in fact, it is crud measure, has an immense contribution to growth. Trade has a long history and economic analysis for the development of a nation. Participating in international trade helps to imitate a new technology and know-how from advanced countries that enable to produce a domestic either new product or in new of the existing product in addition to its role of enabling countries to specialize in its traditional comparative and absolute advantages or the modern competitive advantages. These are the traditional definitions of trade. Whereas trade has been intervening in the socio-political spheres of the globe.



Graph 3.7: Openness $\{(ex + im)/GDP\}$, 1994-2018

source: own graphics

Graph3.7 above presents the openness measured by the most common import plus export as a share of gross domestic product. This measure has various economic implications. Primarily, it measures how much did the GDP growth is contributing to the trade balance of the country i.e. either import or export. The type of causality between trade and growth varies in type of product and economic policies type followed by that specific country. As shown in graph8 above, the ratio has a relatively increasing trend up to 2005 from 0.27 in 1994 to 0.55 in 2005. The annual average for this period is about 0.37. After 2000 the ratio has linearly increased until it comes back to the lowest of the period to 0.38 of 2009 world crises. The rapid increase could be attributed to moderate enough rain and better agricultural production of the period.

Again as shown above in graph3.5 at this period there was a huge debt inflow. From these two, we can conclude that Ethiopian trade has a strong relation to foreign shocks and domestic shocks. It slightly recovered from the 2008/9 crises and back to decelerating after 2011's peak of 0.55.

3.5 Methods of privatization in Ethiopia

The privatization proclamation gives the full power of determining the modalities of privatization for the agency. The method of privatization has a significant effect on the impacts of privatization. Different studies found different results for the various modalities of privatization. In the analysis of modalities of privatization, the domestic conditions and circumstances of the economy play a significant role. This includes the political system existed, distribution of income, objectives of privatization, valuation methods to mention some. In Ethiopia, privatization stated as the revenue-generating mechanism for other development activities, re-directing the balance from the public lead to the private and encouraging the private sector, management-employee buyout, 100% share sale and total sale are dominantly utilized. For the seek of simplicity the privatization contractual price of SOWs enterprises presented in categories and annually starting from 2012 due to data limitations.

Table 3.1: Annual group privatization contract prices in modalities

Year	Modality	Contract price (in birr)	year	Modality	Contract price (in birr)
1994-1999	total sale	420,337,346	2006-2011	total sale	3,929,775,698
	business sale	1,540,167		MEBO	3000100
	MEBO	46,524,602		Lease	108,839,145
	Sale of asset	27,182,194		100%share sale	8,983,611,643
	concession	1,290,429,153		Unspecified	743,325,000
	Sub-total	<u>1,786,013,462</u>		Sub-total	<u>27,537,103,172</u>
2000-2005	total sale	859,329,170	2012	-	3,246,329,362
	Sale of asset	2,212,549	2013	-	2,187,679,213
	lease	2,917,297	2014	-	2,129,032,935.8
	100% share sale	9,153,155	2015	-	1,249,290,516.5
	joint venture	1,254,000,000	2016	-	1,343,660,900 □
	Sub-total	<u>2,127,612,171</u>	2017	-	130,000,000
		Sub-Total	-	<u>10,285,992,927.3</u> □	

Source: Own computation from the Ethiopia Privatization Agency

As shown from the table 3.1 below, privatization has increased nominally. Given the inflation of the country, the nominal value of privatization has increased from 1.786 billion birr in 1994-1999 to 2.128 billion birr in the period 2000-2005. Privatization has grown at about 19.123 percent from 1994-1999 of the starting time to 200-2005. In the first period of 1994-1999, the concessional privatization method dominated the others accounting for about 72.25% of the total sale followed by the total sale and MEBO 23.54 %, 2.6 % of the total sales respectively. In the second period 2000-2005, the methodology has been changed from the dominant concessional sale to no concessional sale. A joint venture has been taking the lion share. It seems the government has been shifted towards the foreign investors as the time was drought and weak agricultural performance and also economic performance explained the economy. In addition to this, as shown above, this is the time of the general government debt to GDP ratio has been peaked. Here we can correlate debt to GDP ratio and privatization for abroad from the graphs and tables presented above. In this period the second-highest privatization method is full sale accounting over 40 % of the total sale next to a joint venture of 58.94% of the total.

The third group of period is part of the global crisis period of 2008/09, but more or less domestically favorable times of harvest. It seems that the government has shifted from a joint venture to domestic investors. Ethiopia was executing the national plan of the plan for accelerated sustainable development to end poverty plan. The country continued privatization progressively, despite the inflation factor is not adjusted, in this period i.e. it grew from the period 2000-2005 to 2006-2011 by 1194.27% in cumulative terms. It is a progressive growth of thousand of percent growth. The 100% share sale and total sale take the first and second rank each accounting at about 32.62 and 14.27 percent in the period. In overall, there is no consistent privatization method, rather it shifts with domestic and international activities, portraying the external pressure with unprecedented and unprepared privatization of the country.

It seems privatization has been declined in the last period of the study. Privatization was the highest in the third 6 years period (2006-2011) of the classified presentation. Although it is difficult to disclose this with other economic performances of the economy, it can be stated in relation to debt and growth of the country. As shown above, in graph 3.2 and 3.4, this is the time after the study periods of ever highest government debt of 2003/04 registered and the country's economic growth has been stabilized since after in relative terms. It accounts for about 66% of the whole privation of the country in the study period.

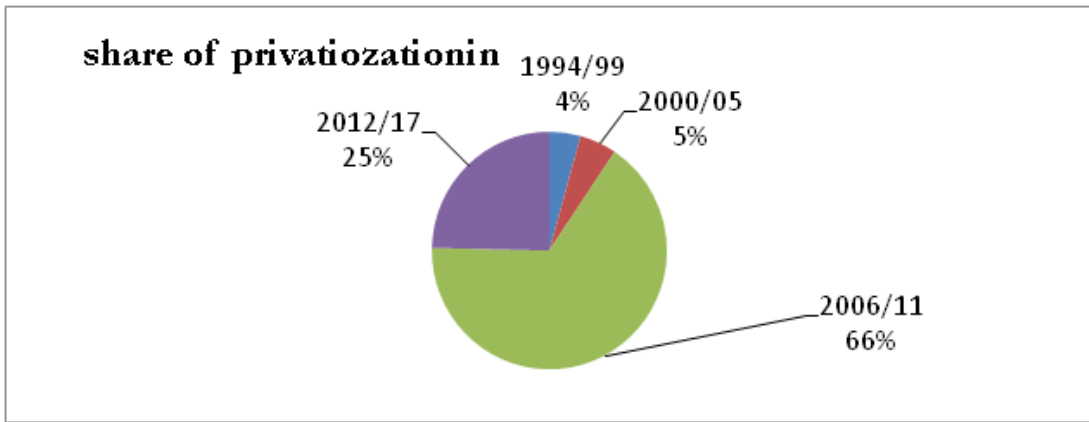


Figure3.6: privatization share in the grouped years

As shown in figure3.1 above, the most significant amount of privatization undertaken in the period 2006-2011 about 66% followed by 25% of 2012-2017. In a 6 years category presentation, it shows an ever-increasing privatization in the country.

Chapter 4

Data and Methodology

4.1 Theoretical Description of the Model

In this section, I will present a simple growth equation based on a theoretical explanation for the empirical analysis of the effects of privatization on economic growth. The model is adapted from Bennett, et al (2004) with appropriate modification to tally with Ethiopian condition. First taking privatization as an argument or policy variable, the real aggregate demand and supply functions are specified. The exogenous variables are selected based on theoretical and empirical explanations. Then combining the demand and supply functions the single empirically testable real GDP equation was developed. Privatization as the main policy variable will be considered with other related determinants of growth of the country. Great emphasis is given for the variable private sector development, trade openness, government expenditure, and government debt effect on growth in addition to the main variable of interest of privatization proceeds.

Weeks and Hailu (2011) suggested policy choices, which they advised to be taken together, in their analysis of developing countries especially post-conflict and resource-rich countries. They advised these countries to focus on the fiscal policies of revenue mobilization, and scaling up public investment. In the monetary policy of financial market development, preventing inflation pressure and stimulate private sector development. On the exchange rate policy, they focused on maintaining slow depreciation and international competitiveness for the stable macroeconomy.

For a given time, the real aggregate demand and supply functions are represented by Y_d and Y_s respectively. Aggregate demand is specified as a function of price and privatization. Taking privatization as a policy variable and real aggregate demand is negatively related to price.

The above variable signs indicate partial derivative effects.

$$Y^d = Y(P^-, PRIV^?) \dots\dots\dots 1$$

Where p represents price, in addition to the negative relationship with price, real aggregate demand is expected to be affected by the privatization policy (PRIV). Despite there is a difference in the method of privatization, the privatization proceeds may be used as finance and not as revenue, which may affect aggregate demand via investment. Mackenzie (1998) argued sometimes privatization reduces the propensity to invest and depresses aggregate demand as a tax increase would. In this analysis, he concludes that, given the difficulty of predicting this when it will happen and its exceptional nature, the receipts of privatization proceeds do not, in most cases, warrant a stance of the fiscal policy to maintain aggregate demand. Therefore, presuming that Ethiopia privatization most focuses on domestic privatization, is expected to distress investment and so growth. Again here, I assumed the unidirectional relation of investment to growth in the nation's economy based on Barro's (1991). On the other side Maitah et al (2016) argued as a result of privatization, the new owners of shares feel richer as they now have more assets, and it raises overall demand for goods. Based on this it is left inconclusive in this stage consistent with different empirical studies results. Here I also assume that firms employ more labor in support of the policy that privatization increases employment and the labor income which in turn aggregate demand.

Real aggregate supply is specified based on the Bennet et al (2004) as follows.

$$y^s = Y(priv^?, PC^+) \dots\dots\dots 2$$

In this study, the main argument is privatization (PRIV) policy's impact on growth. The process of privatization aiming in generating a strong private sector by restricting the government's hand from the economy for creating a sustained and stable economy should include the analysis of the business environment. The private sector contribution (PC) to economic growth is assumed to affect growth positively and significantly. In the privatization policy analysis using two groups of variables is very important. Consistent with other studies of Cook and Uchida, (2001, 2003) and Bennett (2004), the use of control variables and policy variables helps to net out the policy variables impact.

In the analysis of privatization-growth linkage- the theoretical and empirical specification of models is new and not full-fledged especially in single country cases despite there are some that enable to undertake. Most of the studies are microeconomic, whereas the macroeconomic studies are in a cross country scenario and sparse in depth. Therefore, the selection of the explanatory variables in this study needs careful selection and a full review of the existing studies. Taking into consideration the above cases, this study used the initial political, economic,

and social control variables consistent with Cook and Uchida (2003) and Bennett et al (2004). The variables competitiveness, government consumption, and government debt are added in the model as control variables. Cook and Uchida (2001) mentioned that the use of government consumption for political corruption or another measure of bad government, as well as for the direct use of non-productive expenditure or taxation.

In the meantime calibrating the private sector development on growth is another concern of the study. Privatization as a process of transferring resources and functions from the inefficient public to the efficient private for economic growth, therefore, should have a channel by which it transmits its positive financial and operating improvement from the micro-firm level to the macro-economic growth. “If the positive effect of privatization per se on the financial performance and productivity of firms predicted by the microeconomic theories obtain, these effects will have a macroeconomic analog raising growth” (Bennett et al, 2004).

The other control variable in this study is external debt held by the government and should be paid by foreign currency. Debt as one of the main sources of finance for developing countries should be controlled in this study to extract the impacts of privatization on growth. Governments may implement privatization at the time of their high debt stress for debt service than promoting growth. Inspecting that external government debt of Ethiopia is included in this model as a control variable. The two debt measures of the debt stock and debt flow should have a different effects on growth and for the motive of privatization. Debt stock could affect economic growth negatively for developing countries of those in high debt accumulation risk. On the other hand debt flow could affect growth positively. The financial flow in the form of debt can enhance investment capacity and henceforth economic growth. In this study, not only it's economic growth but also to filter out debt causality for privatization, debt stock measure is used. The government may undertaking to service its ever-accumulating debt stock.

The level of trade openness of a nation by how much did the specific nation interacts to the outside world. The measure import and export as a share of GDP is the best proxy measure for trade openness and is most commonly used. In this study I will try to calibrate the contribution of external trade relation to growth in association to privatization. That is in addition to the econometric analysis the causality test indicates the direction of causality between privatization and openness in support of privatization for the expansion of the export by the presumed efficient private sector.

$$Y = \beta_0 + \beta_1 PRIV + \beta_2 GOC + \beta_3 OPP + \beta_4 GODB + \beta_5 PC \dots \dots \dots 3$$

The variables government external debt GODB, and government consumption expenditure GOC, are control variables.

Consequently, the econometric model to be estimated is specified;

$$Y_t = \beta_0 + \beta_1 PRIV_t + \beta_2 GOCT + \beta_3 OPP_t + \beta_4 GODB_t + \beta_5 PC_t + \epsilon_t \dots\dots\dots 4$$

4.2 Definition of Variables

In a time series analysis of the growth impacts of privatization, a simple augmented growth model is specified. The dependant variable of interest economic growth is measured by the real gross domestic product growth. The uses of a constant price wipe out the inflation effect in each variable. It is in 2010 constant price which extended for each variable. Privatization proceeds is measured by the annual proceed as a share of gross domestic product consistent of the previous uses by Cook and Uchida (2001, 2003), Plane (1997), and Barnett et al (2000). Final government consumption expenditure and government debt are used as a share of gross domestic product. The private sector development variables of the private share of the national income measured by the final private expenditure share from a national accounting identity. The trade openness is measured by the ratio of the sum of import and export to gross national product. This measure of countries' competitiveness and external exposure to copy imitate or learn new technology and improve its products to enhance growth has been used in different studies.

4.3 Data

As mentioned above, in this study I exploit a time series data on macroeconomic variables of Ethiopia for a period of 25 years since the first privatization undertaken in 1994. The data set used in my study is retrieved from an online database of World Bank (for the real GDP growth, import, and export), IMF-world economic outlook (for general government gross and net debt stock and flow), National Bank of Ethiopia (for government consumption expenditure), Ministry of Finance and Economic Cooperation (for a private share of the GDP) and Ethiopia Privatization Agency (for privatization proceeds). In addition to this different time publications are also used in the study.

4.4 Econometric Model

Based on the above-specified model, this study will retrieve the most parsimonious time series analysis, which will fit with the data that I am going to use. Conducting the entire tests, like stationery, level of co-integration, serial correlation, the functionality of the model, normality, heteroscedasticity and the cumulative sum of recursive residuals (CUSUM) or the cumulative sum of recursive square (CUSUMSQ), an Error Correction Model (ECM) has been specified.

Stationary Test: before conducting any econometric analysis, test for stationary of each series for the study period should be undertaken. The cointegration analysis of time series data for the stochastic trend is ever increasingly in use since the seminal work of Engle and Granger (1987) and test for unit root is necessary before turning to cointegration analysis, non-stationarity is prerequisite for adding variables for cointegration and long-run analysis. The level unit root test modeling is as described as follow;

$$\Delta Y_t = \mu_0 + \mu_2 \Delta Y_{t-1} + \sum_{i=1}^p (\beta_i \Delta Y_{t-i}) + \varepsilon_t \dots \dots \dots 5$$

Where Y is variable to be tested; Δ first difference operator; μ_i (for $i = 1$ and 2); and β_i (for $i=1, 2 \dots p$) constant parameters; and ε_t is the stationary stochastic process. P is the maximum lag length to be chosen by the Akaike information criteria AIC or Schwartz/ Bayesian information criteria SBIC to ensure that ε_t is white noise.

Thus, the test hypothesis is formulated;

H0: $\mu_2=0$, i.e. there is unit root-the series is nonstationary

H1: $\mu_2 \neq 0$ i.e. there is no unit root-the series is stationary

If the calculated ADF test statistics are less than the Mackinnon's critical values or if the Mackinnon P-value is higher than 5% we can't reject the null hypothesis this means that there is a unit root problem between Y_{t-1} and Δy_{t-1} . This implies the series is not integrated of order zero i.e. I (0). This leads to a test by differencing until it becomes stationary. If it becomes stationary at the first difference, the series is integrated of order one i.e. I (1). The rejection of the null hypothesis implies the absence of unit root and the variable is integrated of order zero. The order of integration of the variables as specified in equation (5) is determined from the standard Augmented Dickey-Fuller test (Dickey and Fuller, 1981) and Phillip and Perron (1988) unit-root tests for the absence of unit root. Then, if the variables are in the same integrated order or integrated of order one and above, the analysis of cointegration proceeds.

The co-integration analysis has done on the main variables of interest; real GDP growth rate, foreign debt stock, openness, private sector share from national income, and privatization proceeds. Following the co-integration analysis of the interest variables, which is if there is a

significant co-integration among the variables, which means there is a long-term equilibrium or equilibrium relationship among the variables. In this step of the study, two alternative models will be selected by econometric tests. The error correction model (ECM) and the autoregressive distributed lag model (ARDL). The test result indicates the existence of cointegration which means there is a system that integrates the short-run to the long-run of the variables. Any deviation from the long run adjusts to the long run by the system that cointegration.

4.5 The Bounds Test for Co-integration

This is the test used to select the right model for the collected time series data incorporating the co-integration analysis. Thus, the test for a hypothesized three variables of X, Y, and Z can be specified like this. ARDL (P, q1, q2) with the hypothesis of the short-run vs. the long-run model. Here p represents the lag length of the dependent variable and q1 and q2 of the exogenous variables lag length. The test is as follows.

$$H_0: \theta_{1i} = \theta_{2i} = \theta_{3i} = 0, \text{ (where } i=1, 2, 3)$$

$$H_1: \theta_{1i} \neq \theta_{2i} \neq \theta_{3i} \neq 0$$

The null hypothesis says that the coefficients of the long-run equation are all zero or insignificant, which implies that, there is no co-integration and specification of the long-run model of ECM. On the other hand, the alternative hypothesis presents that all the long-run coefficients are different from zero and there is co-integration of the variables. This enforces us to specify the long-run model. The most common and parsimonious cointegration test Johansson test of cointegration is conducted to conclude that there is a system that adjusts the economy from the short-run to the long-run; there is at least one cointegration equation in the model.

Despite the test is necessary for the selection of the model, almost all macroeconomic variables are non-stationary at level. Thus, in this step of the model, the error correction model is developed.

If there is co-integration or long-run relationship among the variables, we can apply an error correction model for the above-specified model as follows. The only difference is the last term of the error correction term, which presents the long-run dynamic result of the model.

$$\Delta LnGRGDPT = \beta_0 + \sum_{i=1}^p \beta_1(\Delta LnGRGDPT-1) + \sum_{i=1}^q \beta_2(\Delta LnGOCT-1) + \sum_{i=1}^q \beta_3(\Delta LnGODBT-1) + \sum_{i=1}^q \beta_4(\Delta LnPRIVt-1) + \sum_{i=1}^q \beta_5(\Delta LnPCt-1) + \sum_{i=1}^q \beta_6(\Delta LnOPPt-1) + \alpha ECTt-1 + \varepsilon t. \dots \dots \dots 6$$

$\Delta LnRGDPt$ = change in Log of the growth of real GDP at time t

$\Delta LnPRIVt$ =change in the log of the privatization proceeds as a share of GDP at time t

$\Delta LnOPPt$ =change in Log of openness measure as a share of import plus export per GDP at t

$\Delta LnPCt$ =change in Log of the private sector contribution to the national product-private consumption expenditure as a share of GDP at time t

$\Delta LnGODBt$ =change in log of the net government debt stock as a share of GDP at time t

$\Delta LnGOCT$ =change in Log of government consumption as a share of GDP at time t

The above error correction model specification, regression results present the short-run and long-run relationships of the variables. $ECTt-1$ is the lagged residual of the co-integrated relationship. It is computed with the normalized long-run coefficients from the co-integrating vector.

$$ECTt-1 = LnRGDPPt-1 + \beta_0 + \beta_1 LnPRIVt-1 + \beta_2 LnPCt-1 + \beta_3 LnGOCT-1 + \beta_4 LnGODBt-1 + \beta_5 LnOPPt-1 \dots \dots \dots 7$$

The coefficient α is the error correction term, which measures the speed of adjustments of economic growth from shocks or the deviation of economic growth from its long-run relationship with the explanatory variables. The coefficients of $\beta_2, \beta_3, \beta_4, \beta_5,$ and β_6 are the measures the short-run elasticities of explanatory variables while β_4 is the interest variable privatization's impacts on the economic growth.

4.6 Diagnostic Tests

Before estimating the above model, I carry out a test for stationarity of the variables in the model using the Augmented Dkfuller test (ADF) and Phillip –Perron test and find that all the variables are integrated of order one, (1) (see in the result section). In addition to this, the test for cointegration by using both Johansen’s (1991) test and Pesaran et al (2001) bounds test shows the existence of co-integration. This justifies the use of an error correction model for the estimation of the specified model. Tests for multi-co-linearity using Variance inflation factor (VIF), serial correlation test using Durbin-Watson, normality using White (1980) test, and homoskedasticity using Bruesch Pagan- Godfrey test and the result shows all are consistent to estimate the ECM model.

The model specification-RESET and model stability CUSUM test results also show there is model stability. The test for omitted variable problem is in a way that the null hypothesis of there is an omitted variable over the alternative of the null is not true. From the test result, the null, H0: no omitted variable; can’t be rejected significantly. The model adjusts to words the long-run after any shocks i.e. the model is table although the speed of adjustment has been found weak.

Chapter 5

Result and Discussion

5.1 Result for Correlation Analysis

The magnitude of privatization measured by the total proceeds from privatization as a share of the gross domestic product has made a significant impact on the various variables of economic growth (Yarrow, 1999). Despite privatization's impact is most in a touch with microeconomic variables, macroeconomic objectives are set to be achieved by the policy. Many empirical studies found that the government budget deficit arises from its excessive allocations for their SOEs, which had not generated revenue that covers the investment costs mainly due to its corrupt and not well-managed operations. Thus, taking a huge share of the government expenditure SOEs are among the factors for government budget deficit.

Ethiopia's budget deficit to GDP ratio, which stood at 0.069 in 1986/87, had jumped to 0.097 in 1991/92 (MoPED, 2003; see Selvam, 2007). This figure declined from 1994 to 0.054 and had jumped again to 0.106 and 0.116 in 1997/98 and 1998/1999 respectively. This time is the eve of the ethio-Eritrean war which is one of the responsible reasons for the soaring military expenditure. Drought was another phenomenon of the time, which triggered the agricultural production of the country and call for the government subsidy or social safety net. In the period 1994-2002, the deficit rate grew at about 0.084 or 8.4 percent until it reaches the maximum of the study period 0.129 in 2002. Since then, it has almost stable and declining trends at an average growth rate of 5% (MoFEC, 2019).

This ratio shows how much the GDP contributes to reducing the gap i.e. the excess of expenditure over revenues. Among different fiscal measures took by the government privatization program and expanding the tax base, in fact questioning their contribution, has a significant role. In the correlation analysis of Pearson correlation analysis and Spearman's rank correlation analysis found a significant and positive correlation between privatization and budget deficit.

Another important variable is external debt, which is at the center of economic debates. Despite different reasons or objective have been stated for borrowing, to finance government budget deficit and for fighting poverty are the most common ones in developing countries. As a developing country Ethiopia has been working in poverty reduction. In the process, government finances by borrowing either from abroad or from home. The external debt pattern had changed into bad fashion after the imperil regime overthrown by the military Derg-regime (Selvam, 2007). According to Selvam during the 17 years military junta time the country's external debt increased by 30 fold owing to its extravagant expenditure on defense and the inefficient SOEs. This soaring trend continued during the next and current EPRDF government to put the country in highly indebted poor countries group. In 2018, the World Bank analysis of the country shows Ethiopia is in high debt risk. In examining the policy's macroeconomic impacts the correlation analysis between privatization proceeds as a share of GDP and government budget balance as a share of GDP, debt to GDP ratio is undertaken and reported below.

Table 5.1: Correlation Analysis Result

Variables	Privatization	Government debt	Government budget deficit	Government consumption
privatization	1.0000			
Government debt	0.3378	1.0000		
Government budget deficit	0.5344*	0.4520*	1.0000	
Government consumption	-0.5453*	-0.2991	-0.6321*	1.0000

The link between privatization and budget deficit external debt has a hot debate by economic policymakers, researchers, and practitioners. Government undertakes privatization to fill its gap i.e. fiscal therapy at the same time to reduce its debt burden on the loss-making state-owned enterprises. As shown in table5.1 above, the correlation between privatization and government budget deficit is positive and statistically significant. The Pearson correlation coefficient is 0.53 and significant at 5%. This result is consistent with the theoretical and empirical thoughts of privatization for budget deficit (see Ramamurti, 1992). To generate sufficient revenue for other development activities of government and avoid the financing of the loss-making SOEs

the government opts to privatize.

The Ethiopian government put the goals of privatization for generating revenue for the undertaking development activities than the revenues from SOEs. Thus, the all times national budget deficit has put a strong pressure on the government to privatize its losing making enterprises. On the other hand, in many empirical studies, it is proved that international donors, especially IFIs; put strong pressure on different countries to privatize in line with the Washington consensus especially in Africa before they prepare themselves for the policy (Ramamurti, *ibid*). In fact, it is found a positive correlation of privatization and government debt albeit its insignificance. The correlation coefficient of 0.34 between privatization and foreign debt shows the pressure of foreign debt accumulation for privatization. But it is not statistically significant and should be taken cautiously.

5.2 Result of Unit Root Test

Before estimating the above model, the unit root test for stationary of each time series is necessary. The concept of stationary is the mean, variance, and covariance of the process is time-invariant. Unfortunately, most often macroeconomic variables are non-stationary. Then, before doing any econometric analysis testing stationarity is common and mandatory. Otherwise estimating non-stationary variable Y_t upon a non-stationary variable of X_{it} may lead to the so-called spurious regression in which the estimators and test statistics are misleading. As a first step, the test for stationarity shows none of the series in levels the null hypothesis of a unit root can be rejected at a 5% level of significance. For the first difference, the null hypothesis is rejected at a 1 and 5% level. Thus, each time series is integrated of order one, $I(1)$. The Davidson and Mackinnon (1993) p-values are used in the determination of significances in addition to the test statistics.

Table 5.2: Result for Unit root tests

Variable	ADF test				PP test				conclusion
	level		Difference		Level		Difference		
	Intercept	Intercept & trend	Intercept	Intercept& trend	intercept	Intercept & trend	Intercept	Intercept & trend	
Lnrgdp	1.76	-1.48	-3.17**	-3.58**	1.57	-1.48	-3.13**	-3.49*	I (1)
Lnpriv	-2.01	-1.89	-5.09*	-5.00*	-2.09	-1.99	-5.10*	-5.01*	I (1)
Lngoc	-1.64	-1.95	-4.49*	-4.35*	-1.73	-2.05	-6.19*	-6.09*	I (1)
Lnpc	-1.94	-1.14	-3.03**	-3.22**	-2.05	-1.38	-2.96***	-3.15***	I (1)
Ln godb	-2.18	-2.99	-6.24 *	-6.14 *	-2.25	-3.04	-6.19*	-6.09*	I (1)
Lnopp	-1.205	-0.771	-3.736*	-3.821*	-1.436	-1.024	-3.718*	-3.78**	I (1)

Note: *, ** and *** indicates the significance level at 1, 5 and 10 % respectively

As shown in table 5.2 above, in both augmented Dickey-Fuller and Phillip and Perron tests the variables growth of real gross domestic product (GRDPP), privatization proceeds as a share of GDP (PRIV), government consumption expenditure as a share of GDP (GOC), trade openness as a share of GDP (OPP), private sector contribution to national income as a share of GDP (PC), and government debt as a share of GDP (GODB) are stationary at first difference. They are non-stationary at level even with trend. After the first difference those variables are stationary becoming integrated of order one, I (1). This gives the stepping stone for the next cointegration analysis and error correction estimation that may proceed to the existence of cointegration.

5.3 Co-integration Test Result

When the series used in the study is non-stationary at level but becomes stationary after differencing that shows there is a long-run relationship among the variables that adjusts the short-run deviation from the long run. The test for co-integration is, therefore, the formal statistical justification of the existence of this relationship among the variables for the long-run equilibrium. Thus, if there is cointegration among the variables there is a systematic relationship that functionalizes the variables to form a linear stationary process that adjusts to the long-run after any shocks or deviation of the short-run.

Table 5. 3: Bounds test result for cointegration

Null Hypothesis: No long-run relationships exist		
Test Statistic	Value	k
F-statistic	6.370392	5
Critical Value Bounds		
Significance	l0 Bound	l1 Bound
10%	2.26	3.35
5%	2.62	3.79
2.5%	2.96	4.18
1%	3.41	4.68

Source: own computation by eviews9

The above table presents the bounds cointegration test that strengthens the Johansson cointegration test of long-run relation of the variables (see annex3). The F-statistic value is larger than any of the values at the zero bound even at 1 percent in support cointegration rejecting the null.

The first step in the Johansen test for cointegration is optimal lag length selection. The test is lag sensitive and adding small lag enables one to reject the null while adding more lags increases the acceptance likelihood. In this study, I used the Akaike information criteria to find the optimal lag length of two. The Johansen cointegration test for the test of the existence of long-run relationships among the variables indicates there is a long-run relationship among the variables. The test statistic presents both the trace statistics and maximum Eigenvalues test with the normalized cointegrating equation. The test based on the null hypothesis of there is at most r number of cointegrations against there is more than r cointegrations sett in the null.

5.4 Model Stability and Diagnostics Test

Before proceeding to a statistical regression analysis of the model different tests should be undertaken to check the fulfillment of different assumptions. After checking unit root test of each series, the serial correlation test (by Brush and Godfrey LM test or Durbin Watson test), multi-collinearity (by LM test and VIF result appended), functional form of the model (by Ramsey RESET) test, normality (Jarque-Berra test) and heteroscedasticity (by Breusch-Pagan) test are reported below. The long-run stability of the estimates has been tested by the cumulative sum of recursive residuals (CUSUM and CUSUMSQ) test.

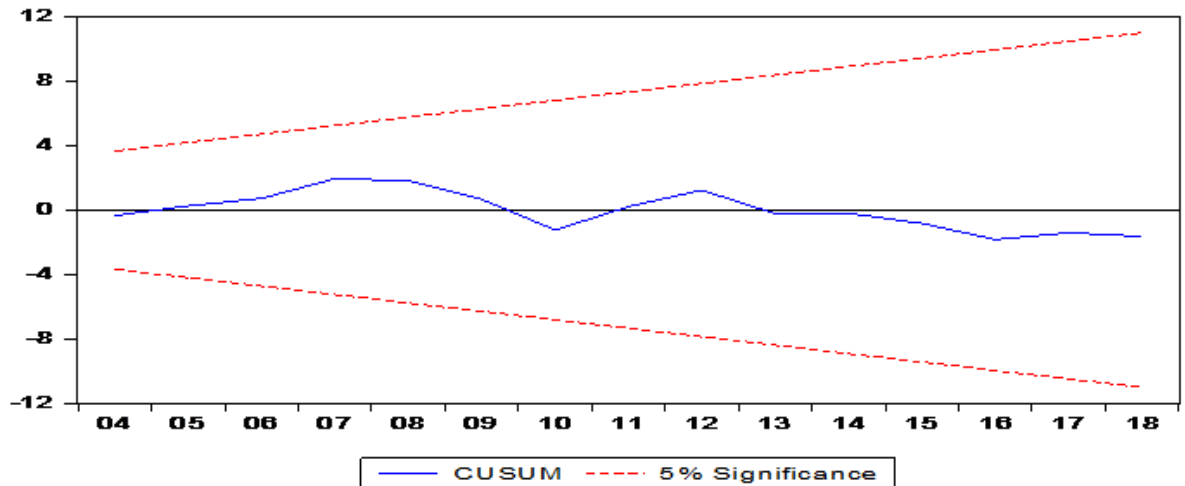
Figure 5.4: Stability and Diagnostics Tests Result

H0: hypothesis	H1: hypothesis	Test type	Chi ² (p≥0.05)	F-stat (P≥0.05)	Decision
No serial correlation	Serial correlation	Autocorrelation LM test	3.22 (0.20)	1.26 (0.31)	accept the null hypothesis
Homoskedastic	Heteroskedastic	Breusch-Pagan	3.55 (0.68)	0.63 (0.62)	accept the null hypothesis
No omitted variable	Omitted variable	Ramsey RESET test	0.02(LR)(0.92)	0.01(0.90)	Accept the null hypothesis
Normally distributed	Not the null	Jarque - Berra test for the distribution of the disturbance	0.53 (0.77)	0.78	Accept null hypothesis

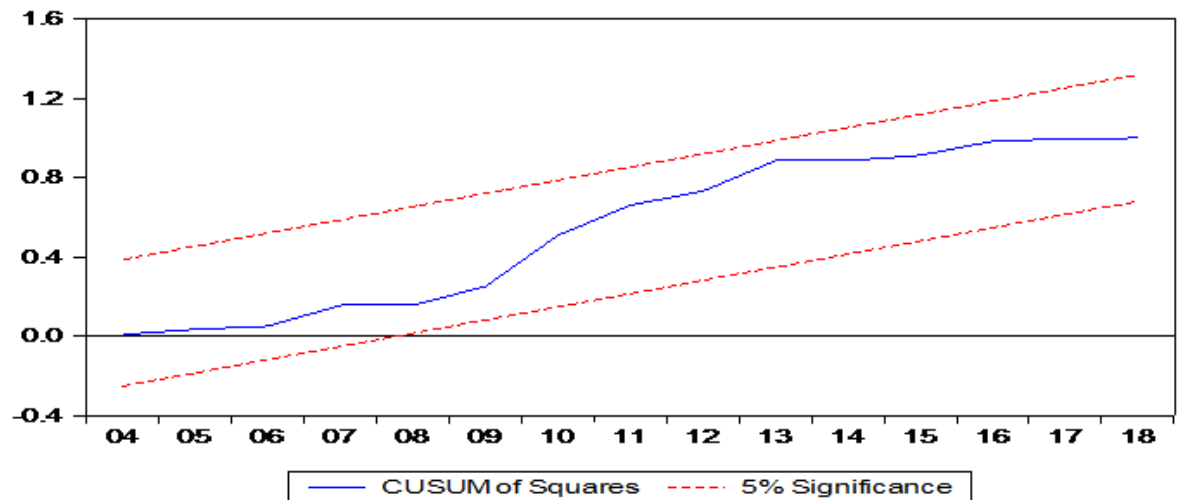
The post estimation test of serial correlation in the null hypothesis of there is no serial correlation over the alternative hypothesis of there is serial correlation has the expected result. As shown in the first row of the table 5.4 above, a p-value is 0.2 for the chi2 of 3.22. This is much higher than 0.05 or even the weak significance level of 0.1. Therefore, we can't reject the null hypothesis of there is no serial correlation. In the second row of the above table, the Breusch-Pagan heteroscedasticity test statistics show the absence of heteroskedasticity. The p-value of the test statistics is 0.68 and 0.62 for F-test and chi2 to accept the null hypothesis of homoskedasticity. The next row is the result of the model specification test for omitted variables problem of the analysis. The hypothesis is there is no omitted variable in the model specification in the null and not the null in the alternative hypothesis. Taking the p-value again

we can't reject the null hypothesis of there is no omitted variable in the model. The normality Jarque-Berra test of the disturbance term found good results. In the same fashion, we can't reject the null hypothesis in favor of the normality of the disturbance term.

After all the short-run and long-run model parameters stability is tested by the CUSUM and CUSUMSQ stability test as presented below. In both CUSUM and CUSUMSQ the graph should be inside the lower and upper bounds for the stability of the long-run parameter as found consistently.



Graph 5. 1: Test for parameter stability-Cumulative Sum of recursive



Graph 5. 2: Test of parameter stability-cumulative sum of square of recursive residuals

Source: eviews9 output

Graph 5.1&5.2 above presents, the test of the stability of the parameters by cumulative sum of recursive residuals shows the model is stable. The red lines indicate the 5% critical

significance level and the blue line shows the fitted models. The graph didn't cross the upper and lower bounds as an indication of the long-run stability of the model. In other words, there is no structural break in the model.

5.5 Error Correction Estimation Result

The results show that the estimated model has a good fit. Error correction model estimation for both the short-run and long-run coefficients simultaneously presented in table 5.5 below. Besides, the model passes all the post estimation diagnostics tests including the normality, heteroscedasticity, serial correlation, model specification, and stability.

Table 5.5. The growth impacts of privatization (1994-2018)

Dependent Variable: $\Delta(\log$ of the Growth rate of Real GDP)			
Variables	Coefficient		t-statistics
Short run			
Constant	63.82		3.16***
$\Delta(\text{Log of privatization to GDP ratio})$	0.22		1.99**
$\Delta(\text{Log of privatization to GDP ratio})(-1)$	0.18		1.68*
$\Delta(\text{Log of private contribution to GDP ratio})$	-1.82		-0.94
$\Delta(\text{Log of trade openness to GDP ratio})$	0.76		1.95*
$\Delta(\text{Log of trade openness to GDP ratio})(-1)$	1.75		2.44**
$\Delta(\text{Log of government debt stock to GDP ratio})$	-2.48		-4.23***
$\Delta(\text{Log of government debt stock to GDP ratio})(-1)$	-0.61		-1.58
$\Delta(\text{Log of government consumption to GDP ratio})$	-2.79		-2.17**
$\Delta(\text{Log of government consumption to GDP ratio})(-1)$	2.01		1.91
Error correction term ^c	-0.66		-2.00**
Long run			
Log of privatization to GDP ratio(-1)	-0.15		1.39
Log of private contribution to GDP ratio(-1)	-7.32		-4.59***
Log of trade openness to GDP ratio(-1)	0.53		1.91*
Log of government debt stock to GDP ratio(-1)	-0.86		-2.65***
Log of government consumption to GDP ratio(-1)	-0.79		-1.59
Diagnostics Tests			
R-squared	0.94	Adjusted R-squared	0.78
Jarque - Berra	0.53	Ramsey RESET test (LR test)	0.02
Jarque – Berra: P(value)	0.77	P(value)	0.92
F-statistics	5.75	Breusch-Godfrey Serial Correlation LM Test:	3.2
P(F-statistics)	0.02	P-value	0.20
		Breusch-Pagan Heteroskedasticity Test(P-value)	0.68

*, **, *** Significant at 10%, 5% and 1 % levels, respectively; ^c The coefficient estimate for the error correction term is also that for the lagged dependent variable.

The coefficient of privatization proceeds to GDP ratio (PRIV) is not statistically significant in the long run with a negative coefficient. However, in the short-run it has a positive sign and it is statistically significant. A similar insignificant effect of privatization on growth has been reported in prior studies for different countries (see, e.g., Cook and Ochida, 2001, 2003;

Ozata 2014). The previous study in Ethiopia has inconclusive results. Selvam (2004, 2007) has found a negative growth impact of privatization while Reddy and Desalegn (2018) found significant and positive short-run and long-run growth impacts of privatization. Thus, supporting Selvam's result the possible reason for the short run statistically significant and long-run negative insignificant growth impact of privatization may relate the fact that in the first place privatization is small in Ethiopia relative to other developed and developing countries and the revenue is used for short term financial demands.

Privatization has found a strong and significant correlation with a budget deficit that supports this result. Similar results reported by Javad et al (2011) explaining the government's short-run plan focus than the long run by using privatization. If the success of privatization is linked to competition and regulation of competition, then weakness in this field may explain why privatization is negatively related to growth in developing countries (Cook and Uchida, 2001). Consistently, Senbet and Wedajo (2018) found a distorted and politically biased competition in Ethiopia and competition policy have shown significant weakness in developing countries (Gray, 1991 cited in Cook and Uchida 2003); cook, 2001).

The effect of private contribution to growth is found to be negative and statistically insignificant in the short run but significant in the long run. Prior empirical studies also found similar results in other countries (see Bennet, 2004; Shukrove et al, 2016). Bennett et al (2007) can't confirm the private sector's development contribution to economic growth significantly. This negative coefficient can be explained by the fact that privatization in particular and denationalization and private sector development, in general, was unsuccessful in creating a competitive environment and level playing field indicating the problem is beyond the property right structure to other structural problems. Despite the long history of the private sector in Ethiopia, almost none during the military regime, it has been in a situation of triggering challenges. After the military regimes fall and the EPRDF government's reform in line with the west capitalist system and adjustment program the privatization and other deregulations transformations challenged by its sensitive nature in terms of politics, economics, and maladministration. Privatization in the industrial sector where over 90% of employment is in public enterprises and the agricultural sectors are the sectors that highly touched by privatization (Deneke, 2001).

In the period 1990 to 2000 out of the total domestic private and foreign investment projects only 31.77 percent were operational in the given eight years and this is severer for the domestic investments where only 32 percent operational achieving only 28 percent of the planned employment opportunities (Deneke, *ibid*). In the meantime, the country lost 60.4 percent of the planned investment for many reasons. This effect is also disappointing in the foreign invest-

ments side where only 16.6 percent of the planned employment opportunity accomplished. The aforementioned factors may be taken as the driving factors of the disappointing private sector development in the country where again private investment challenges are readily apparent. Those ethnic slanted politically decided investments are not paying us back rather adding up the delinquency of the politics.

The competitiveness measuring variable of trade openness's coefficient is as expected positive both in the short run and long run and significant in the short run only. Trade openness hastens the process of globalization in helping countries to imitate or copy new technologies, specializes in a product that particular country has a competitive or comparative advantage, and also smoothing the socio-political and other institutional and cultural interactions. The channel through which the positive impacts of trade openness passes to economic growth depends on the level of bargaining, politico-economical development, and institutional absorbing capacities. Despite the aforementioned factors with the applied methodological differences cause divergence in the impact of trade openness on economic growth, in this study, it has found both positive impact and significant effect on the growth of Ethiopia consistent to the prior studies in Ethiopia and abroad (see Keho, 2017; Haylun and Getie, 2019).

Debt stock is found to have a statistically significant and negative effect on real GDP growth both in the short run and long run as expected. Debt is used as one of the major sources of finance for developing countries; perhaps the debt overhang problem has to mix up those countries the economic status of those which didn't keep debt sustainability. The above result is found in different countries' studies in developing countries. Government consumption impacts growth negatively as expected. Government consumption as a measure for political corruption or other measures of bad government, as well as for the direct use of non-productive expenditure or taxation (Cook and Uchida, 2003) has found the expected sign of negative both in the short run and long run but significant only in the short run. This has an important implication for the status of the economy that the real problem includes inappropriate government expenditure.

Chapter 6

Conclusion and Recommendation

6.1 Conclusion

This study has explored the short run and long-run macroeconomic impacts of privatization in Ethiopia using a time series data for the 1994-2018 period, focusing on the growth, fiscal, and debt impacts and relations of the policy. A simple economic growth model was developed where the policy variable of interest privatization controlled by the government debt stock and government consumption in addition to the effects of external competitiveness and private sector development augmented the model. Before the regression analysis is conducted the Pearson pairwise correlation was computed. The national budget deficit has a statistically significant correlation with privatization consistent with the stated hypothesis. On the other hand debt to privatization correlation has found low and insignificant that the debt burden and international donor organizations' debt conditionality for privatization premises failed to be supported in Ethiopia. The potential reason may relate to its late starting of privatization and some extent of government resistance. One surprising result is the positive and significant correlation between privatization and trade openness. The result from the econometric analysis of the macroeconomic impacts of privatization shows that its growth impact is significant in the short-run only concerning financing for the most heightened deficits and but negatively, in the long run, losing its statistical significance. As Machenzie (1998) found privatization only affects aggregate demand in the case of privatization used as revenue but not as a short term financing. By reducing the debt burden or national deficit privatization revenue can impacts growth positively in the short run but not for a long time. On the other hand the overwhelmingly targeted private sector development for the sustained and stable economy of the country, failed to reap the grapes of the mimicked developed countries. The private sector in Ethiopia is characterized by the duopoly of ruling party paras-

tatals and family business conglomerates creating a special business environment in worsening the productivity and efficiency potential gains for the pace of economic growth (Wedajo and Senbet, 2017).

Foreign debt stock affects growth negatively due to the debt overhang problem of the country is in high debt risk and it is positive in its flow measure financing the investment demand. Trade openness as one of the pillars of privatization in the process of the competent private sector has found a positive impact but significant in the short run only. Therefore, privatization in Ethiopia doesn't have any significant growth contribution even in private sector development. Despite it needs more studies taking more institutional and political variables, this result should be taken cautiously. For this, the government consumption variable has an important implication for the need for more studies.

6.2 Recommendation

Privatization as one of the transition policies of the government targeting generating revenues for the other development activities, strengthening the private sector, and restricting the government's hand from the economic production and provision to regulation and supervision activities in Ethiopia is unsuccessful. In this argument, there is one important assumption that the private sector is efficient contrary to the public inefficient. This assumption fails to account for both the theoretical and empirical concept of efficiency which importantly depends on the economic environment and level of competition that prevails in the economy not only on property rights. This is what other prior studies and I found in this study. Based on this it is better to work more on the structural problems of the country like corruption, creating a level playing field for private-sector competition, export expansion, and improve the business environment before privatization. The current COVID-19 pandemic tested advanced countries and it is apparent for developing countries. Financing the fight against the pandemic is among the heightened challenges that demand power full and strong government both for current containing of the pandemic and its long-run consequences. Thus government should halt its privatization plan not only for the welfare of the public but also for himself to stay in power.

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Appendix

Annex1: Test for multicollinearity by Variance inflation factor

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. vif
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Variable	VIF	1/VIF
LNOPP	2.63	0.380048
LNPRIV	2.25	0.445241
LNGODB	1.79	0.558438
LNGODB	1.22	0.822056
LNPC	1.10	0.911088
Mean VIF	1.80	

Annex2: The Granger causality test result

LNPOPP does not Granger Cause LNPRIV	23	0.16953	0.0454
LNPRIV does not Granger Cause LNGODB		3.68653	0.0455
LNOPP does not Granger Cause LNPC	23	3.20503	0.0645
LNPC does not Granger Cause LNOPP		0.35174	0.7082

Annex3: Johansson test for Cointegration

Trace test

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.949870	180.1981	95.75366	0.0000
At most 1	0.891773	91.3559	96.81889	0.6401
At most 2	0.771411	40.21494	47.85613	0.2302
At most 3	0.500658	26.27090	29.79707	0.1208
At most 4	0.358629	10.29824	15.49471	0.2585
At most 5	0.003596	0.082865	3.841466	0.7734

* denotes rejection of the hypothesis at the 0.05 level

Maximum Eigen Value

Unrestricted Cointegration Rank Test (Maximum Eigenvalue)

Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.**
None *	0.949870	68.84220	40.07757	0.0000
At most 1	0.891773	31.14101	33.87687	0.7260
At most 2	0.771411	23.94403	27.58434	0.6778
At most 3	0.500658	15.97266	21.13162	0.2265
At most 4	0.358629	10.21538	14.26460	0.1982
At most 5	0.003596	0.082865	3.841466	0.7734

* denotes rejection of the hypothesis at the 0.05 level