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I Z A
World of Labor
Evidence-based policy making

Impact of privatization on employment and earnings

Workers and policymakers may fear that privatization leads to job losses and wage cuts, but what's the empirical evidence?

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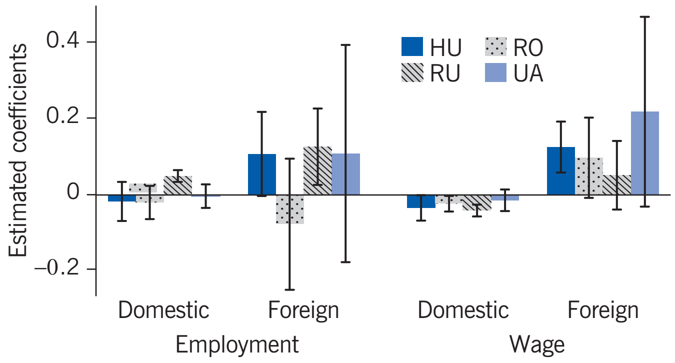
ELEVATOR PITCH

Conventional wisdom and prevailing economic theory hold that the new owners of a privatized firm will cut jobs and wages. But this ignores the possibility that new owners will expand the firm's scale, with potentially positive effects on employment, wages, and productivity. Evidence generally shows these forces to be offsetting, usually resulting in small employment and earnings effects and sometimes in large, positive effects on productivity and scale. Foreign ownership usually has positive effects, and the effects of domestic privatization tend to be larger in countries with a more competitive business environment.

Privatization, especially under foreign investors, can have positive effects on employment and wages



Source: [1].

KEY FINDINGS

Pros

- State ownership and central planning are generally thought to be associated with excess employment.
- Soft budget constraints and lack of competition under state ownership may lead to rents for incumbent employees.
- Private owners are likely to aim for profit maximization rather than political objectives; they may have access to skills, markets, and technologies that increase output, employment, and productivity.
- Productivity increases may lead to wage increases.
- Positive effects are more likely the larger the scale and productivity effects, which may be greater under experienced, skilled investors in better business climates.

Cons

- Budget constraints are not infinitely soft, so state-owned firms have some incentives to economize.
- Negative consequences for employment and earnings are larger where state-owned firms are most protected, regulated, and subject to planning.
- The business environment and intensity of competition matter regardless of ownership.
- Limited evidence suggests that wage and employment losses are greatest for low-skilled workers.

AUTHOR'S MAIN MESSAGE

Until recently, employment and wage effects of privatization received little attention in empirical research. None of the conducted studies show large negative effects on either employment or wages. Recent research in transition economies using much larger panel data that enable use of more appropriate evaluation methods confirms this finding and also reports systematically better outcomes for workers under foreign than domestic privatization. The policy implications are potentially profound. Despite the likely performance benefits, policymakers may be reluctant to privatize because of fears of job losses and wage cuts. The findings that average employment and wage losses tend to be low and that effects are sometimes positive should alleviate those fears.

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