Causes and Impact of Privatization in Nepal: A Theoretical Review

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ABSTRACT
During and after 1950s when private investment was not common due to the infant corporate culture, Nepal adopted an inward-oriented development strategy that emphasized import-substituting industrialization with the state playing a dominant role. This led to the establishment of number of public enterprises which largely assisted the country develop its industrial, professional, and institutional base. However, they could not perform as per the expectations thus giving way to the privatization efforts after 1990. The article reviews the literature available both at national and international level to identify the causes and impact of privatization particularly in the context of Nepal. The reviewed literatures are presented using content analysis. The available literature broadly categorizes the causes of privatization in Nepal as Domestic and International. Furthermore, the literature reveals more favorable than unfavorable cases so far as the impact of privatization is concerned. An attempt has been made to understand the impact of privatization efforts on economic, social, political and environmental fronts in the past couple of decades. The paper concludes with a note that a massive awareness program targeted at educating all the stakeholders about the benefits of privatization will further help trickle down its benefits among the general masses.

Keywords: Public Enterprises, Privatization, Globalization, Privatization Act

JEL Classification Codes: L32, L33, O16

1. INTRODUCTION

1.1. Background

Privatization, the most significant economic, social, and political phenomena (Miller, 1997) was adopted on a worldwide scale in the 1980s, covering both rich and poor countries, large and small nations, and governments subscribing to the full spectrum of ideologies (Ramamurti, 1992). The ideological considerations - exemplified by such statements as, "governments have no business to be in business" - have often been paramount in driving privatization in various parts of the world. Lieberman (1993) views privatization of public enterprises (PEs) not an end in itself, but as a critical element of economic adjustment. The poor financial and operating performance of PEs has necessitated privatization and thus is viewed as a possible remedy to overcome the malaise of the public sector as it will reduce the role of the state, lessen the state's fiscal deficit by decreasing the demand for continued financing of firms from the exchequer, and improve the asset quality of the banking system.

The campaign for privatization internationally dates back to the early 1980s, after the election of Margaret Thatcher in Britain in 1979 and Ronald Regan in the United States in 1980 (Monem, 2006). Well known examples of privatization include the sale of firms like British Telecom, British Gas, and Japan Airlines to millions of small investors, and the sale of the Chilean state-owned airline or the Mexican telephone company to multinational enterprises and foreign investors (Ramamurti, 1992).

A notable economist Joseph E. Stiglitz argues that privatization entails the conversion of enterprises formerly controlled by the government into private hands (Stiglitz, 1992). Similarly, Narain (2003) defines privatization as the rollback of the state in the lives and activities of citizens and strengthening the role of markets; however in the narrow sense, it refers to the transfer of ownership from the public to the private sector or transfer of control over assets or activities as in the case of privatization through leasing, where ownership is retained, leaving management of assets and activity to private parties. Savas (1989) sees privatization as the act of reducing the role of government or increasing the role of the private institutions of society in satisfying people's needs; it means relying more on the private sector and less on government. It denotes mainly the divestiture of public assets to the private sector; nevertheless, a broader view tends to encompass processes such as denationalization, deregulation, liberalization, contracting-out, competitive tendering, user charges, cuts in public provisions, increases in private ownership, and so on (Hartly and Parker, 1991; Martin, 1993; Murie, 1994). Privatization, therefore, indicates a transfer mainly of the carrying out of those activities that are economic in nature, either in whole or in part to the private sector, that were formerly carried out in the public sector through different modalities.

Government pursue privatization in order to promote increased efficiency, introduce competition, expose public enterprises to market discipline, encourage foreign investment, foster wider share ownership and raise revenue for the state (Megginson, 2000). Vickers and Yarrow (1988) observe that privatization as a policy has been adopted with the following aims:
- Improving efficiency;
- Reducing the public sector borrowing requirement;
- Reducing government involvement in enterprise decision making;
- Easing problems of public sector pay determination;
- Widening share ownership; and
- Gaining political ownership.

I. W. Lieberman, a World Bank senior consultant and privatization expert, has argued that the following six factors have influenced the adoption of privatization as a critical feature of countries' economic policies (Lieberman, 1993):
- The successful economic performance of Japan and the Newly Industrialized Countries (NICs, like Korea, Singapore, Hong Kong and Taiwan);
- At the time the growth model of Japan and the Asian NICs was proving so successful, there was growing awareness that other models for economic development, such as the command economy, had outlived their usefulness and needed to be rejected;

- The fourth industrial revolution, driven by information-based technologies, which requires competitiveness;
- The role of PEs, which have monopoly status and have bred inefficiency and a lack of competitiveness;
- In the 1980s advanced industrial countries such as the USA and the UK expressed a strong ideological commitment to private enterprise; and
- Since 1989 the political revolution in Eastern Europe and the Soviet Union has lent new impetus to the privatization process, as the newly emerging democracies in most of these countries are utilizing privatization as a cornerstone of their economic reform process to create the basis for a market economy.

Gopal Joshi in his article Overview of privatization in South Asia has identified three general reasons for pursuing privatization as: greater economic democracy through increased private initiatives in economic activities; achieving higher levels of economic growth and employment; reducing budgetary deficits (Joshi, 2000). It is now widely accepted that the success of privatization depends on the maturity of the institutions in the market economy, including legal frameworks on property rights, private contracts, dispute resolution mechanisms, and rules of entry and exit for business enterprises. For privatization programs to be sustainable, however, they need to be properly understood, taking into account the interest and perceptions of all stakeholders (Calabrese, 2008).

Privatization can therefore be thought of as a tool to drive the process of liberalization by putting private sectors at the forefront with the presumption of increased efficiency and thereby to gradually reduce the role of government in the economic decision making. But making a case for privatization entirely on the experiences of western countries where the outcome of the process were largely positive may be unfavorable for the least developed countries where serious bottlenecks persists which are more of a non-economic nature for e.g. bad governance.

1.2. Public Enterprises in Nepal

Public enterprise is identified with three characteristics. First, they are classified as part of the public sector and so must be owned by the government. Second, they are an enterprise and therefore must be engaged in the production of goods and services for sale. Third, sales revenues of PEs should bear some relation to cost (Paudel, 2006).

During 1950s, the private investment was not common due to the infant corporate culture and Nepal adopted an inward-oriented development strategy that emphasized import-substituting industrialization and accorded a dominant role to the state in the articulation and implementation of the strategy. As a result, from the sixties to the early eighties, there was an upsurge in the establishment of PEs which expanded from a mere holding in a commercial bank in early 50s to a total number of 63 public enterprises by the end of mid 70s. A report on performance of privatized enterprises (1999) spelt out following six objectives of establishing PEs:

- To stimulate economic activities in the country as there is absence of significant role-play by the private sector in this regard;
- To avail goods and services to the general people at fair prices and in abundant quantity;
- To create employment opportunities in the organized sector;
- To substitute imports and save foreign exchange;
- To utilize the foreign aid; and
- To develop economic and social infrastructure.

Most of the PEs came into existence during Second, Third, and Fourth Plans in the 1960s and first half of the 1970s and have permeated to almost all sectors of the economy, namely, manufacturing, public utilities, banking, trading, and social services. The table (Table 1) shows expansion and then by contraction of PEs during different plan periods which Manandhar (1993) in his PhD thesis has further divided into four periods as: i) growth period (1952-1975), ii) period of reconciliation (1975-1980), iii) period of restraint (1980-1990), and iv) promise of privatization (after 1990).

Table 1: Growth of public enterprises in different plan periods

Periodic Plan	Total number	Change
Prior to 1956	1	-
First Plan (1956-61)	8	7
No Plan period (1961-62)	11	3
Second Plan (1962-65)	22	11
Third Plan (1965-70)	34	12
Fourth Plan (1970-75)	61	27
Fifth Plan (1975-80)	59	-2
Sixth Plan (1980-85)	54	-5
Seventh Plan (1985-90)	63	9
No Plan period (1990-92)	62	-1
Eighth Plan (1992-97)	46	-16
Ninth Plan (1997-2002)	43	-3
Tenth Plan (2002- 07)	36	-7

Source: Paudel, 2006 (original data from NPC)

1.3. Privatization Efforts

With the objectives to increase productivity by improving efficiency reducing administrative and financial burden of the government and increasing private sector participation as well as by ensuring effectiveness of service delivery, the process of privatization, dissolve and liquidation of government-owned PEs started since 1993 (Economic Survey, 2009). As per the privatization law, PEs can be sold according to the following modalities: sale of assets and business, sale of shares, and sale-cum-lease. In the former case, the enterprise is liquidated and its assets are sold. In the second case, the firm is not liquidated and its shares are auctioned. In the third case, the business is sold and the assets are leased for 10-35 years (Privatization Act, 1994).

The disinvestment of 30 public enterprises have been completed by FY[1] 2008/2009 using different modalities such as liquidation, dissolving, management contract, selling of assets and businesses, partial selling of shares, selling of current assets and building, and leasing out of properties (Appendix 1). Out of 36 PEs, 7 are in the industrial sector, 6 in the trading sector, 7 in the service sector, 5 in the social sector, 3 in the public utility sector, and 8 in the financial sector (Economic Survey, 2009).

This study, therefore, tries to divulge various national and international causes that led to the initiation of privatization efforts in Nepal focusing on economic and political causes including pressures from development partners and the wave of globalization. Similarly, the study also tries to evaluate the economic, social, political and environmental impact of about 'two decade' of privatization efforts. The study concludes with few recommendations to improve the effectiveness and efficiency of the privatization efforts being made in Nepal under the aegis of globalization and liberalization.

2. METHODOLOGY

This study is entirely based on secondary sources of information - literature review has been conducted in order to collect information on various aspects, including causes and impacts of privatization in Nepal. The major literature comprises of studies after 1990, after which the Nepalese economy saw a major economic reform process under the aegis of globalization and liberalization. Similarly, in order to present and analyze the reviewed studies, content analysis is conducted. In content analysis data are categorized under topic headings and all responses are kept under respective headings. As such, the study is conducted by agreeing upon the main theme and sub-themes emerging from the information.

3. RESULTS AND DISCUSSIONS

3.1. Causes of Privatization: Pre-Privatization Analysis

The establishment of PEs had greatly assisted in the country's industrial and professional development, and helped to prepare the necessary institutional base; however, the PEs could not perform as per the expectations and underwent a series of anomalies. The mounting loss, political interference, frequent changes of board membership and of the chief executive officer, mismanagement, low technical know-how, shortage of capital, over staffing, and poor financial management, including poor accounting and record-keeping, are the subject of frequent and justified criticism. To accelerate the pace of national development it has become necessary to increase efficiency in the areas through proper and efficient management. Together with this it has become necessary to bring about changes in the structural framework of the corporations in order to enhance the standard of services rendered by them. As, the performance of these institutions remained weaker during the most part of the last two decades, it ultimately necessitated the economy to adopt the Structural Adjustment Program (SAP) of the World Bank (WB) and International Monetary Fund (IMF) in 1980s; and so a condition to it, the government initiated the privatization efforts.

Nepal's Privatization Act (1994) defines privatization as involving private sector in the management of the, or to sell or lease it, or to transfer government ownership into public ownership, or an act to infuse participation by any means, either wholly or partly, of private sector or of the employees or workers, or of all desirous groups. Regarding the cause of privatization, the preamble of the Act mentioned:

> "Whereas, in order to increase the productivity through enhancement of efficiency of the state owned enterprises of the Kingdom of Nepal[2], and thereby, mitigate the financial administrative burden to the Government, and to usher in all round economic development of the country by broadening the participation of private sector in the operation of such enterprises, it is expedient in the national interest to private such enterprises and to make arrangements thereof."

The causes of privatization can be studied under two categories as domestic and international causes. The domestic causes are the indigenous internal causes which exerted pressure of privatizing the enterprises. On the other hand, international causes are related to the pressures imposed by development partners of the country, and impact of globalization.

3.1.1. Domestic Cause

The domestic causes relates to the internal factors paving path for privatization which can be further split up into economic and non-economic causes where by economic causes are the ones which have adversely affected the economy in relation to profitability, sustainability, and production, among others. Non-economic causes are related to the political causes.

3.1.1.1. Economic Cause

Economic causes relate to the need of increasing institutional performance, improving financial management, generating additional revenue base, and encouraging domestic and foreign investment which fueled the need of privatizing the enterprises.

Increase Institutional Performance: Different studies (Manandhar, 1993; Manandhar and Bajracharya, 2000; Paudel, 2006; Paudel, 2009; Economic Survey, 2009) univocally identified that PEs in the country were dismal performer ascribed to the lack of commercial orientation, inadequate autonomy, poor accounting and accountability, managerial inefficiency, low technological know-how, overstaffing with inappropriate skill mix, subsidy dependent, corruption, mis-utilization of resources, and negligence, which has led to additional vicious financial burden to the state. The poor performances of PEs have often been attributed to weak management practices of the heads of these institutions, as the heads were not appointed based on competencies but on political connections, which has seriously compromised commercial underpinnings and bolstered managerial inefficiency. It was felt that doing business is not the business of the government because it does not have the required skill, capacity, and orientation to handle the business as properly as the private sector does. Therefore, it is expected that privatization will increase the productivity of PEs and, this in turn, will help to create more employment opportunities, better wages and working conditions, lower prices and better quality (Manandhar and Bajracharya, 2000).

Reduce Financial and Administrative Burden to the Government: The sluggish and fragile performance of PEs have drained national treasury via loan and high subsidy. According to Economic Survey (1992), up to the FY 1990/91, Nepal Government had invested a capital of Rs. 6,303.2 million and loan investment worth Rs. 15,584.2 million on the existing PEs. The PEs which were audited in the FY 1989/90 showed a loss of Rs. 240 million, which increased up to Rs. 1,870 million in the FY 1990/91. From this, it has been evident that PEs has become a perpetual financial burden to the government. As the average capacity utilization of these enterprises was only 52 percent and had mostly gone into loss, the capital grants to be given by government for functional and transportation expenses gradually increased to Rs. 76,720 million in the FY 1990/91.

The PEs are still exerting financial burden to the government, that can be seen in the recent Annual Performance Review of Public Enterprises (2009) which states that most of the enterprises are operating at loss and some have negative net worth. Economic Survey (2009) explicitly mentions that 17 corporations have earned net profit, whereas 19 corporations made losses during FY 2007/2008. Moreover, these enterprises are creating unfunded liabilities for gratuity, pension, provident fund, and medical expenses ultimately resulting in economic burden to the government.

Clearly, there has been increasing financial burden on the government due to PEs. Since it has become necessary to enhance the working efficiency, to effect managerial reforms and to run these enterprises from the commercial point of view, it became necessary to analyze the future of these enterprises and to privatize them.

Likewise, PEs were imposing high administrative burden to the state. Though PEs are autonomous self governing units, their supervision, and monitoring and evaluation responsibilities rest with the government. Ministry of Finance through its Corporation Coordination Division supervises budgetary allocation and approval, performance monitoring and evaluation. Moreover, administrative burden also implies periodic recruitment of chairman, board of directors and general managers, which also invites public criticism of political patronage, appointments and interference in the management of PEs.

According to Sharma (1995), the problems that the public enterprises faced were:
- Management had no commercial managerial ability or dynamism, and had a public service mindset under which they ‘administer’ rather than ‘manage’ the companies;
- Corporations were tied up by various rules and regulations which led them to lack necessary flexibility and, hence, the competitiveness;
- There is lack of technical expertise, even in the basic areas such as accountancy, labor management, and production planning;

- There was an absence of responsible fiscal management and no sense of responsibility to either the government as the shareholder, or to other creditors;
- Over-manning was practiced at every level and was particularly acute in the 'administrative' grades;
- There was no consideration for the interest of the consumer; and
- There was no consideration for the interest of suppliers or the people with whom the enterprise does business.

Generate Additional Revenue Base: According to Bennett (1997), one of the goals of privatization is fiscal stabilization, such as maximizing proceeds of sales, reducing the future drain of subventions and capital contributions from government revenue, increasing tax revenues from higher profits and reducing the public debts. Generating revenue was regarded as one of the objective of privatization as perceived by Koirala[3] government (Sharma, 1995). It was thought that privatization helps injecting capital in the social sectors by increasing revenue and investing in sectors such as water, electricity, education, and health.

Encourage Private Investment: Private sectors whether nationals or internationals are considered as the niche of the time as they are believed to be more efficient so as to maximize profit and minimize cost of production. However, the level of private investment in the country was negligible and the major commercial holdings were state undertaking till 1980s, which was operating at huge losses and thus had become as white elephant to the government. Therefore, encouraging and attracting private sector and foreign investors was considered quite essential and hence privatization was thought to be the stepping stone in this regard.

3.1.1.2. Non-Economic Cause

Political Cause: During the 1980s there was a remarkable change in Nepalese economic policy, thereby, liberalizing its economy to facilitate the private sector and a competitive market system (Paudel, 2009). The movement in 1990 saw a U-turn in the country's political system from Partyless Panchayat System[4] to multiparty democracy. This change in the political system also affected its economic policy. The Koirala government of early 1990s published a white paper called Policy Paper on the Privatization of Public Enterprises in 1991 which clearly aimed to introduce a balanced approach between the public sector and private sector (Ibid). In 1994, Privatization Act was enacted. All administrative decisions were made within the jurisdiction of the Act, whereby the government took decisions on the recommendation of the privatization committee whether to privatize the PEs. The formulation of industrial policy and the commercial policy in 1992 also generated fertile ground for the smooth implementation of the privatization policy. The economic policy of the Nepalese government is moving towards a new trend of liberalized economy, giving major roles to the private sectors in both the manufacturing and service sector.

3.1.2. International Causes

International reasons relate to the external forces that were dominant forcing the country to adopt privatization in practice. One of the prominent causes might be the coercive pressure imposed by the development partners in the name of sanctioning the loan. In addition, it might have happened because of the voluntary adaptation of international policy and/or due to the impact of globalization, which Nepal felt and so acted accordingly via privatizing.

3.1.2.1. Pressure from Development Partners

The collapse of socialism in the former Soviet Union countries led the new paradigm shift from socialist economy to the market economy which dramatically decreased the role of the state worldwide. The market-oriented economic thinking in the West entailed the promotion of privatization by powerful international agencies, such as the WB, IMF, and the Asian Development Bank (ADB), usually as a part of larger structural adjustment packages favoring private business interests (Monem, 2006).

Given this international context, coupled by the serious macro-economic imbalances in the form of growing fiscal deficits and dwindling international reserves, Nepal embarked on a major program of stabilization in 1985-86, supported by the IMF standby arrangement and Structural Adjustment Program (SAP) financed by the WB's Structural Adjustment Credits (Gurugharana, 1996). The leverage of the government to resist conditions by the IMF and the WB became weaker because of the deterioration in the balance of payments; hence the government had no option but to accept the IMF stabilization program to obtain international credit (Khadka, 1991). It is evident that it is necessary to be 'creditworthy' in order to obtain loans from the IMF and the WB, as the loans are not free. One condition of the loans was the reform of PEs due to their disappointing performance compared to the investment. Hence Nepal has accepted privatization policy as one of the conditions imposed on economic reform (Rimal, 1996; Khadka, 1991). The programs were designed to liberalize the economy, improve public sector efficiency, and encourage private sector involvement in agriculture, forestry, trade and industry, reducing the scope for state intervention. Thus, while examining the period of 1985-90, it is found that the policies adopted were extremely based on WB/IMF conditionality included in the SAP.

3.1.2.2. Globalization Impact

Globalization and the concept of global village indicate the interdependence between the countries and it became a common belief that national interest on the economic front can be enhanced through interaction with other countries of the world. Nepal's step towards economic liberalization in the early 1990s was an attempt to be committed to the global world and thus it can be argued that one of the reasons why privatization policy transferred in Nepal is the global economic trend, which demands that every country be competitive on an international level (Paudel, 2009).

3.2. Impact of Privatization: Post-Privatization Analysis

Privatization has been advocated primarily as a means of improving the performance of public sector enterprises. It is frequently argued that privatization may have a significant impact on performance efficiency, financial efficiency, and distributional efficiency (Cook et al., 1998). Nepal has exercised privatization efforts in past couple of decades, the impact of which can be studied on economic, social, political, and environmental fronts. How are the privatized enterprises performing? Do the privatization efforts succeed in attracting private investors from home and abroad? Has employment opportunities increased after privatization? Are the ongoing labors (in terms of facilities provided) and consumers at large (in regard of prices and quality of goods) benefited after privatization? How environment friendly are privatized enterprises? These are the few questions which are attempted to be addressed in the following section.

3.2.1. Economic Impact

Like the economic causes, the economic impact focuses on the privatized enterprise performance, its fiscal management, domestic private investment and foreign investment in the country.

3.2.1.1. Institutional Performance

Production, product diversification, technological improvement and profitability situation are discussed further to understand institutional performance of privatized enterprises in general.

Production: It has been observed that capacity utilization and efficiency of privatized enterprises have increased which has led to the increase in output of such enterprises. For example in Uganda, only 10 percent or less capacity of most manufacturing firms were utilized before privatization which has now increased after privatization observing almost more than tenfold increase in output (Ddumba-Ssentamu & Mugume, 2001)**.** A study by Paudel (2006) on four privatized enterprises namely Harisiddhi Brick and Tile Factory, Bhrikuti Paper Mills, Nepal Foundry Industry, and Biratnagar Jute Mills Ltd. revealed that performance of privatized enterprises are in a good state as the production and sales had increased, however those enterprises failed to increase their profits. Manadhar and Bajrachrya (2000) also view that except few closed enterprises, the outputs of privatized units have increased which means that there is increment in capacity. There is also a perceptible change in the quality of outputs. For example, Harishidhi Bricks has introduced floor tiles in its production line while Nepal Bitumen has introduced emulsion products.

Product Diversification: Many privatized enterprises have been able to increase substantially the availability of commodities often resulting into reduced prices. Ahmed (2000), therefore, rightly mentions that product diversification is a reflection of dynamic entrepreneurial behavior and market-sensitive enterprise restructuring which should have favorable effects on the overall enterprises efficiency. According to the report on performance of privatized enterprises by MOF (1999), the privatized industries have diversified their production to certain extent. Nepal Foundry Industry, for example, has succeeded to diversify its products. Before privatization, it was producing cast iron products but after privatization the company is producing, along with cast iron, manganese steel, hyper steel, hycrome steel, and stainless steel products. The types and quality of products have also increased. Moreover, it is also found that the export potentialities have increased after privatization, as for instance, Bhrikuti Paper[5] exports pulp paper to India while Leatherage Bansbari exports wet blue leather to India.

Technological Improvement: Owing to increase in capital, investment and the capital labor ratio in privatized firms, they are more likely to switch to a more capital intensive technology (Okten & Arin, 2006). Introduction of new technology and better conditions in the production process rather becomes a necessity than choice for such firms in the post-privatization scenario. A necessity to perform better to maintain competitiveness and to improve efficiency to reap the benefits of economies of scale remains the major driving force to adopt upgraded technology. In Nepalese case, some better privatized PEs has done better in terms of technology improvement. For example, Bhrikuti Pulp and Paper Ltd. have started use of waste paper as raw materials and have replaced coal by rice husks, which is very cheaper in comparison of coal. As the smoke of rice husk is less harmful than the coal smoke, it has become more environmental friendly too.

Profit/Loss Situation: Financial performance indicators especially profitability have been found to increase significantly in many countries. The evidence shows that greater and faster efficiency gains in competitive industries have mainly led to such significant gains in financial performance indicators (Ernst et al., 1999). In Bangladesh, the proportion of profit yielding enterprises jumped from 38 percent (out of 195) to 60 percent after divestiture (Ahmed, 2000). Similarly, the gross profit margins more than doubled in the entire eight sample enterprises that were privatized (Haque, 1999). In other South Asian economies also, profitability of the privatized units have been shown increasing. However, in the case of Nepal, most of the privatized units suffered accumulated losses such as Bhrikuti paper Mills, Biratnagar Jute Mills[6], etc (Poudel, 2006). Except few smaller units like Nepal Bitumen, Lube oil and Nepal Foundry, most other privatized units are under financial strain (See: Appendix 2). This may be due to market conditions, production technology, and source of financing and management rather than ownership per se. However, if the profit and loss situation of privatized units is to be compared with the profit-loss situation immediately before privatization, many enterprise have been able to reduce losses, if not increase profit (Manandhar and Bajracharya, 2000).

3.2.1.2. Fiscal Management

It is most commonly argued that the fiscal impact of a privatization is neutral since the value of enterprise - measured by the discounted future cash flow stream - is the same under government and private management (Adam et al, 1992). This notion contradicts with some other modern thinkers' as they are preoccupied with the perception that privatization adds value to the enterprise with the better management and marketing technology and varied incentives by the private sector. If investors bid for the assets according to their valuation, the fiscal impact would be positive (Ernst et al, 1999). Moreover, privatization has also been used as a means of reducing the fiscal burden of the government and lessening the need for external borrowing (SCOPE, 1997). Nepal also had the reduction of financial burden of the government as one of its major objectives of the privatization program.

Economic Survey (2004) mentions that after implementation of the privatization policy, operating subsidies have increased but capital subsidies have been reduced. However, the government is not providing subsidies to at least 24 privatized enterprises and it has collected revenue by selling the PEs. In addition, this has relieved the government of managing the PEs, as the government was responsible for appointing the board of directors before the privatization. This has helped to divert the scarce government resources to other social sector of the country.

3.2.1.3. Domestic Private Investment

Privatization in the country is accused to be supply driven with the government choosing a unit it wants to privatize rather than being demand-driven, that is, selecting those units for privatization that the private sector is willing to acquire. This has created a problem on the part of investors to invest in the units that does not fall within their priorities. Similarly, low number of interested investors in the bidding process also limits the possibility of huge and diversified investment. This may be due to the information gap that the government failed to disseminate through various marketing/advertising tools using popular national and international media sources. However, studies such as by MOF (1999) and Manadhar and Bajracharya (2000) have shown that the private sector investment has increased due to privatization because of the conditionality that requires the private sector to augment production capacity or to restructure or renovate the production process. In addition, the impact of increased investment in terms of enhanced production and efficiency, technology adoption, returns etc have also been quite positive. This benefit, therefore, largely outweighs the cost arisen from the limited number of investors during the bidding process.

3.2.1.4. Foreign Direct Investment (FDI)

Nepal has made a promising start in implementing market-oriented reform and promoting FDI, but it has a long way to go in reaping the benefits from integration into the global economy through FDI. The size of the market is quite small and so the volume of profit is not attractive to lure foreigners. Moreover, the escalation of the civil war has severely disrupted FDI inflows to Nepal since late 1990s and as a result most foreign investors have ceased their operations, as they become target of a Maoist rebel group (Athukorala and Sharma, 2006). Despite the fact that Sri Lanka remained in the civil war for about three decades (more than that of Nepal), but still it had successfully attracted foreign investment, for instance, Japan was attracted in the telecom of Sri Lanka, national airlines of the Emirates for the Air Lanka and Hanjung the largest steel producer of Korea to steel company[7]. In case of Nepal, although FDI in Bhrikuti Paper and Leatherage Bansbari has been noticed, however, the amount was not significant. It can be said that mere liberalization of the investment regime and the introduction of financial incentives are not substitutes for an all-encompassing effort to improve the investment climate. Nepal has failed to attract FDI through privatization.

3.2.2. Social Welfare Impact

Social welfare impact relates to relevant actors in the economy, including the workers and consumers and how are they benefited or harmed by privatization.

3.2.2.1. Employment

One of the prerequisites of privatization in Nepal is a guarantee of continued employment, provided the worker agrees to work for the private employer. Similarly the labor laws give some protection to workers with regards to job security. Accordingly, laborers employed in the private sector enjoy a fair measure of security of tenure. Taking into account this legal protection, it seems that the workforce to be transferred to the private sector may have job security (DEAN, 1998). But many observers fear that privatization will cause major job losses as new owners of privatized companies shed excess labor to improve efficiency and as divesting governments cut the workforce to prepare for privatization (Cheng, 2008). Studies also show bleak experience of privatized units on employment fronts in South Asian region. Almost 40 to 50 percent of the privatized units in Bangladesh closed down after privatization (World Bank, 1993; Sen, 1997); six public sector units closed subsequent to privatization in Sri Lanka (Salih, 1999); and the closure of four units after privatization in Nepal led 3200 people jobless (Manandhar and Bajracharya, 1999). However, if the closed units are excluded and total employment figures are analyzed, then the total effect comes out to be marginal. In this respect, the 'quantity effect' of privatization on employment gets neutralized which is also true in the case of Nepal. Moreover, Manandhar and Bajracharya (2000) shows that the 'quality effect', in the case of Nepal, to be more severe than quantity effect - the 'no redundancy clause 8' could not ensure job security to the workers with middle level people like administrators, accountants, supervisors suffering more from the job losses from the initiatives of the new managers to curtail the personnel cost; the growing tendency amongst new managers to go for contractual, temporary, daily wage, piece rate wage hiring in privatized units; neutral effect on salaries and benefits ; deterioration of labor relations etc are few examples of such effects.

Paudel (2006) also concluded on the similar lines - he found that the net impact of privatization on the number of employment is negative as about four-fifth of privatized enterprises have reduced the number of employees, but only about 18% of privatized enterprises created more jobs. However, the studies so far been made could not directly attribute these layoffs to privatization for example, it cannot be said whether closures of privatized units was because of privatization or some other factors.

3.2.2.2. Employee Related Facilities

In case of India, privatization led to exploitation as regular jobs were converted into low paid jobs depriving the workers social security and other essential benefits like housing, medical, and children's education (Goyal, 2000). Manandhar and Bajracharya (2000) reports that there has been a further deterioration in worker exploitation, working hours, leaves, job security and union activities in Nepal - workers perceive that the social security situation have further degraded. In some cases, the targeted ones do not receive the facilities as stipulated in the Privatization Act 1994 intended to mitigate privatization related labor problems for example the trade union leaders buy all the allocated shares meant for the workers and the common non - party affiliated workers though the Act stipulates that the workers should be allotted five percent of the total shares at a discount of 25 percent payable on an installment basis. Similarly, while privatizing the Agriculture Tools Factory, 65% of its total shares were sold to workers of the company. Although the whole phenomenon looked as workers buyout, however in reality by bidding the company on behalf of workers, outsider people were taking the advantage of concessionaire bidding fee of Rs. 10,000 applicable to workers. This ultimately led to the dispute between investors closed down the factory. Paudel (2006) also attributed poor working conditions and reluctance of new management to take them into new environment as the main reasons for employees to quit their jobs.

3.2.2.3. Consumer Satisfaction

The article limits the concept of consumer satisfaction in terms of price and quality of goods.

Price of Goods: Price of goods of privatized units has shown to be increased in many countries. This may be due to the fact that government protection initially provided to these enterprises such as subsidies are removed and in the initial periods prices tend to rise. However, in the long run when the enterprise competes with other firms with the increase in technological and managerial efficiency the price tends to fall down. A study in china by Lu et al. (2007) suggest that the privatized enterprises were able to seize the opportunity right away to adopt a leaner and more efficient management system, immediately enjoying a decrease in the costs of government ownership. But Nepal had contrasting experience with price of most of the privatized enterprises increasing. In some cases, like bricks and textiles, the price has increased by more than 50 percent. Manandhar and Bajracharya (2000) blame inherent inefficiency of public sector pricing policy for this abrupt increase in price subsequent to privatization.

Quality of Goods: Studies have shown that the quality of goods produced by privatized units has improved vis-à-vis the goods produced by state owned enterprises. Public enterprises in developing economies are characterized by intense government intervention, obsolete technology, overstaffing and constant political interference that impairs the quality of goods produced by such enterprises. Bureaucratic structure of such enterprises does not help promote entrepreneurship in the staffs as well - they are accustomed to accumulate wealth without work. On the other hand, the improvement in technology of production has enhanced the quality of products after privatization. For instance, technology improvement is seen in Nepal Film Development Company. As the services such as dubbing, final mixing, etc were not available before privatization; the producers had to visit India for this purpose. But after privatization, all sorts of services are available in the Company's studio. This new arrangement has reduced the length of time, the total cost involved, as well as the foreign exchange requirement.

3.2.3. Political Impact

It can be said that on the name of privatization and private sector development, there has been tremendous political patronage to friends and relatives of ruling parties. This is supported by controversies over the valuation of the privatized enterprises. As privatized units hold immensely unutilized assets in the form of real estate (the valuation of land has been a critical issue), the valuation controversy seems to have occurred in almost all privatized units. The Annual Report of the Auditor General (1998) has accused that eleven enterprises have been sold off, on an average, with an undervaluation of 29.29 percent. Moreover, there are also cases where PEs has been sold at less than their liquidation value. Thus, the government has been accused for its improper approach to issues such as: undervaluation of the sold enterprises; lack of transparency; and improper and unbalanced utilization of the revenue generated from the proceeds of the sick PEs (Adhikari and Adhikari, 2000).

3.2.4. Environmental Impact

Prizzia (2002) proposes that development and privatization have both positive and negative consequences in environmental administration - negative consequences are often masked or go undetected as the effectiveness of development and privatization is based primarily on economic performance. As such, he recommends that the measures of social as well as economic performance and the overall effect on natural environment should be considered to obtain a more accurate and realistic determination of the effectiveness of privatization. In the case of Nepal, although environmental problems are there, it is difficult to attribute this problem entirely to privatization. MOF (1999) in a report on performance of PEs reports that in some privatized enterprises such as Bhrikuti paper and Pulp, Harisiddhi Brick and Tile, Bansbari letherage etc, environmental issues have been a serious concern whereas in some such as Nepal Film Development Company, Balaju Textile, Nepal Bitumen and Barrel etc, environmental problem has not been added after privatization. Those enterprises reporting to pollute environment after privatization may have been doing so before privatization as well; difference may be in that no such serious attempts to study environmental problems were made before privatization. Moreover, a case can be made that the technological improvements in many of these privatized units may have further helped to reduce environmental problems. It can thus be said that privatization have had less impact to worsen the environmental quality, if any.

4. CONCLUSIONS

The establishment of PEs had greatly assisted in the country's industrial and professional development, and helped to prepare the necessary institutional base. However, the PEs could not perform as per the expectations and encountered a series of anomalies. Domestic and international causes forced the country to privatize PEs. The reviews of the past studies have shown more favorable cases for privatization as against the unfavorable ones.

The impacts of privatization are found to be positive so far as its effects in economic fronts are concerned - it has been able to increase the production with diversification, improve technology, reduce the losses, reduce the fiscal burden of the government, increase private sector investment, increase the quality of goods and services etc. However, the sustainability of these progresses amidst the current political upheaval remains a debatable issue. In addition, although, the number of employment fell in the post-privatization era, this may be regarded obvious as it is principally acceptable for the private sector to resort to such retrenchments to remain cost-effective. So far as low FDI is concerned, there is a need of separate empirical analysis to show that privatization is the only factor affecting the inflow of FDI in the country. When the business and investment environment have not been able to improve due to structural constraints, primarily due to the armed conflict in the recent past and instable government and relentless load shedding as of now, it is but natural that the foreign investors are not attracted to invest in Nepal. Although, prices of the goods might have increased, this cannot be made a stronger case against privatization so far as it comes with enhanced quality. Moreover, when the prices of all goods and services are increasing out of inflation, we cannot out rightly reject this possibility in the goods of privatized enterprises. However, on the name of privatization and private sector development, there has been tremendous political patronage to friends and relatives of ruling parties. On the environmental front, the effect has been shown to be neutral although, again, the environmental deterioration cannot be directly attributed to the privatization and further the pollution might have been a problem with PEs as well.

It is now, therefore, a high time that a massive awareness program should be launched to educate the general people, labors, leaders, and policy makers regarding the advantages of privatization. Before privatizing enterprise, labors and trade unions should be educated about the possible consequence of privatization on their job security, working conditions, and their rights and obligations in the enterprise so that the new management and labors work in harmony. Training and readjustment of labors may be required to deal with redundant labor because of privatization. On the other hand, the new management should be given flexibility to choose its crew in the pursuit of maximizing performance. To attract the domestic and foreign investment, the government should provide some financial, legal, as well as procedural facilities and incentives. Privatization is no means of unloading the burden of the government, in the sense that government will have no responsibility in the future. Training and orientation to the new management is essential to give an impression that the government is committed to privatization for the private sector development. Proper regulation and monitoring mechanism are also strictly needed for environmental protection.

The recent experience with privatization is not so encouraging in Nepal. Although privatization process has been slowed down recently, the performance of the already privatized units has grossly suffered primarily because of labor issues, scarcity of raw materials, and long hours of load shedding. For example, Bhrikuti paper Mills, the largest paper mill in the country and privatized in 1992, have already announced its closure. As such, privatization needs to be managed to ensure transparency, equity, and fairness and consideration must be given to its impact on workers, employers, owners and investors, consumers, management, and all other stakeholders (Martin, 2000). Monem (2006), in his book 'Politics of Privatization in Bangladesh: Western Solutions, Eastern Problems' (citing the World Bank report) pointed out three political ingredients for the successful implementation of privatization or PEs reform as: political desirability, political feasibility, and political credibility of the ruling politicians. The presence of these three ingredients is seriously missing in the context of Nepal. The need of the time is, therefore, to mitigate the negative impacts of privatization so as to make it vibrant and successful.

5. NOTES

[1] FY = Fiscal Year; Nepalese calendar is slightly different from the western one i.e. the English calendar. Fiscal year starts from fourth month, shrawan (that corresponds to July/August), and ends on third month Ashad (that corresponds to June/July).

[2] Now the Federal Democratic Republic of Nepal

[3] Girija Prasad Koirala (20 February 1925 - 20 March 2010) was Prime Minister of Nepal for four times.

[4] Declaring parliamentary democracy a failure King Mahendra carried out a royal coup in 1962. The panchayat system constitutionalised the absolute power of the monarchy and kept the King as head of state with sole authority over all governmental institutions, including the Cabinet (Council of Ministers) and the Parliament.
(See: http://en.wikipedia.org/wiki/Kingdom_of_Nepal#Royal_Coup_by_King_Mahendra accessed 21 December 2009).

[5] However, the Annual General Meeting (AGM) of Bhrikuti Paper Mill held on October 2011 have already endorsed the special proposal of the management to close down the factory citing the shortage of raw materials, power-cuts and decline in the demand of paper etc among others (http://www.myrepublica.com/portal/index.php?action=news_details&news_id=39547). Recent alterations such as these will not be taken into consideration for our purpose.

[6] Biratnagar Jute Mill was closed in 2009 as it was long been lumbering with low output and repeated closures due to inadequate capital (http://www.gorkhapatra.org.np/rising.detail.php?article_id=19988&cat_id=27). The GON is, however, considering to bring the Mill back into operation (http://www.worldjute.com/jute_napal/news.html).

[7] See: http://www.nepalnews.com.np/contents/englishmonthly/businessage/2000/Feb/cover.htm

[8] No redundancy clause: At the time of transferring the services of, and gratuity and other benefits accrued to the workers to the enterprise of the new investor ensure the continuity of service of the present workers enterprise to be privatized. If continuity of service could not be maintained and the present employees and workers of the enterprise have to be retrenched, then there should be arrangement of reasonable compensation or benefits in respect of the present employees and workers being retired from the privatized enterprises (Privatization Act 1994).

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Appendix 1

Table A1: Disinvested, Dissolved and Liquidated Public Enterprises

SN	Name of the Public Enterprises	Year Privatized	Mode of Privatization	Sold Share Percentage	Selling Price (Rs. '000)
1	Brikuti Paper Factory	1992	ABS	-	229,800
2	Harisidhhi Brick and Tile Factory	1992	ABS	-	214,830
3	Bansbari Leather Shoe Factory	1992	ABS	-	29,854
4	Nepal Film Development Company	1993	Share Sales	51.0	64,662
5	Balaju Textile Industry	1993	Share Sales	70.0	17,716
6	Raw Hide Collection and Processing Centre	1993	Share Sales	100.0	3,990
7	Nepal Bitumen and Barrel Industry	1994	Share Sales	65.0	13,127
8	Nepal Lube Oil	1994	Share Sales	40.0	31,057
9	Nepal Jute Devt. & Trading Company	1993	Liquidation	-	-
10	Tobacco Development Company	1994	Liquidation	-	-
11	Nepal Metal Factory	1996	Share Sales	51.0	14,473
12	Raghupati Jute Mills	1996	Share Sales	65.0	82,204
13	Nepal Bank Limited	1997	Share Sales	10.0	125,140
14	Agriculture Project Service Centre	2001	Liquidation	-	-
15	Nepal Tea Development Corporation	2000	Share Sales	-	-
16	Biratnagar Jute Mills	2002	MC	-	-
17	Himal Cement Industry Limited	2002	Liquidation	-	-
18	Cottage Handicraft Sales Emporium	2002	Liquidation	-	-
19	Nepal Coal Limited	2002	Liquidation	-	-
20	Hetauda Textile Industry	2002	Liquidation	-	-
21	Nepal Transport Corporation	2002	Dissolved	-	-
22	Butwal Power Company	2003	Share Sales	75.0	874,200 and US $1million
23	Brigunj Sugar Factory Limited	2003	Liquidation	-	-
24	Agriculture Inputs Factory Limited	2003	Liquidation	-	
25	Bhaktapur Brick Factory Limited	2004	ABS	-	14,500 (asset sale) 31,900 (10 years lease)
26	Lumbini Sugar Factory	2006	ABS	-	78,600 (asset sale) 4,211 (per year rent)
27	Nepal Rosin and Turpentine Industry	2006	ABS	-	110,100 (asset sale) 3,012 (per year rent)
28	Agriculture Lime Industry Limited	2006	Liquidation	-	-
29	Nepal Drilling Company	2006	Liquidation	-	-
30	Nepal Telecom Limited	2008	Share Sales	8.53	4,264,139

Note: ABS=Asset and Business Sale; MC=Management Contract; (Source: Economic Survey 2009)

Appendix 2

Table A2: Profit/loss situation: Before and after privatization

Privatized units	Before privatization *	After privatization *
Nepal Lube	+0.60 (1993/94)	+5.38 (1997/98)
Nepal Bitumen	+0.68 (1992/93)	+3.07 (1997/98)
Leatherage Bansbari	-2.23 (1992/93)	+1.13 (1997/98)
Nepal Foundry	+3.88 (1995/96)	+0.83 (1998/99)
Nepal Film	-4.81 (1992/93)	+0.25 (1997/98)
Bhrikuti Paper	+8.70 (1991/92)	-228.00 (1997/98)
Harishiddhi Bricks	+0.04 (1991/92)	-20.28 (1995/96)
Bhaktapur Bricks	-12.25 (1995/96)	-7.50 (1997/98)
Raghupati Jute Mills	-75.30 (1991/92)	-3.18 (1997/98)
Balaju Textile	-1.20 (1991/92)	-0.21 (1997/98)

Note: *Rs. in Million; (Source: Manandhar & Bajracharya, 2000)