Privatisation – Weighing the evidence

Posted on 07/03/2018 by MetroPolis

Kevin Albertson, Manchester Metropolitan University, Business School, Professor of Economics. Studies Social Policy, Econometrics, and Applied Econometrics.

Dr Kevin Albertson is an eclectic economist with a background in statistics and economics, but now he has escaped from the numerical world of Econometrics into the applied worlds of: Behavioural Economics; Economics and Crime – he is co-author of the critically acclaimed text book 'Crime and Economics: An Introduction' –; and the analysis of government policy.

Last week in a Metropolis **blog** Dr. Chris O'Leary argued against nationalisation. In this blog Professor Kevin Albertson offers a response to Dr. Chris O'Leary and looks at the evidence for and against privatisation

The historical context

Most of us are familiar with the UK government's privatisation programme of the 1980s – **said by the *Economist* magazine to be Britain's most successful export** (even while pointing out that the privatisation of railways had been a disastrous failure).

A primary motivation for privatisation was the need of the government of the day for ready money to boost the economy in a time of recession, while at the same time keeping a lid on public sector debt and taxes. However, as the programme developed, the underlying theory developed also. **Privatisation was sold to the UK public also as a means of making UK business more efficient and further as a means of developing "Democratic Capitalism"**, under which citizens would also have a capitalist stake in the nation. Privatisation was also, of course, pursued for purely ideological reasons; many held to the belief that the public sector simply ought not to own industry, irrespective of its relative efficiency.

Motivations and evidence

Raising Funds

According to the WTO, the UK government realised in excess of US$80 billion from public floatations between 1980 and 1996. This was far in excess of the more measured approaches of other OECD nations. In this period, the UK accounted for 40% of the total proceeds of such policy. This money, along with the **billions raised from North Sea Oil and Gas** revenues and further billions raised from "**Right to Buy**" – the effective privatisation, at a discount, of much of local government's "council housing" – gave central government the means to spend its way out of the recession of the early 1980s while maintaining the narrative of cutting taxes and reducing borrowing.

In this sense then, privatisation was a limited success. Limited in the sense that more money could have been raised because assets were often offered at a price below market price.

Making business more efficient

A second supposed objective of privatisation was to make business more efficient. This is no straightforward objective. We must bear in mind that what is efficient for an individual business is not necessarily efficient for the economy as a whole. It was for this reason many of the free-market economists of the 1930s and 1940s supported nationalisation of key utilities and transport. They considered only democratic accountability – *i.e.* public ownership – will prevent natural monopolies from exploiting the public. Recent history indicates their concerns had some merit. Such is the strength of the current narrative of overcharging by privatised utilities sectors, the cold-war political-economic policy of a price cap has been recently been resurrected by both the UK's main political parties.

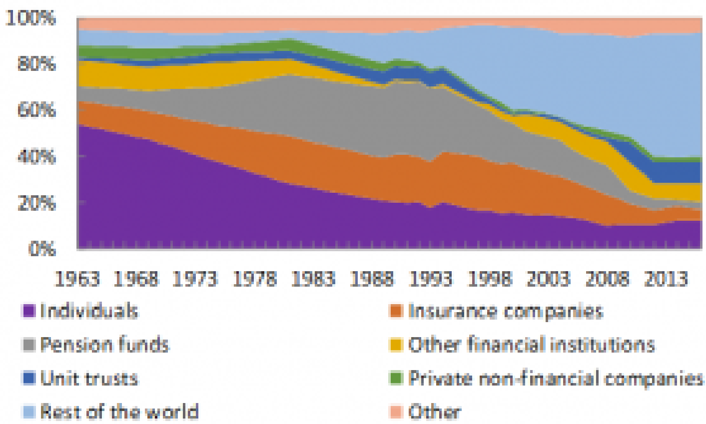
Overall, there is scant evidence of efficiency gains or of benefit to the customer arising from privatisation. The publicly owned Scottish Water, for example, has bills 10% lower than the (privatised) English average water bill.

Spreading share ownership

Tell Sid, ran the advert used to encourage the public to buy into the privatisation of British Gas. However, there are few Sids; the ownership of the nations privatised industries has largely passed out of the UK into foreign hands.

It is not just privatised industries, of course; the majority (54%) of UK quoted shares are now in foreign, mostly North American, hands. UK based individuals, which might include Sid, retain a mere 12%, which is still four times greater than the proportion held by pensions companies (3%). Looking back over half a century, there is no evidence at all that the decline in the proportion of UK quoted shares held by UK individuals was halted, or even slowed, by the privatisations of the 1980s (or since).

Percentage of total market value of UK quoted shares by sector of beneficial owner



Bringing it all back home?

Given the apparent failure of privatisation to live up to its promise, other than to furnish central government with short-term funds, it is hardly surprising that **Sid, and the majority of his fellow Britons, would rather national utilities and infrastructure were run by the public for the public**.

This does not mean re-nationalisation is economically viable (**other than the railways, where all the government need do is let franchises lapse**). In the first instance, the profitability of privatised utilities makes their repurchase very expensive. Consider, for example, the water industry. In 1989, the then government made £3·6 billion from its sale (£37·6 billion in today's money). To buy it back now would **apparently cost £90 billion**. This represents an average real rate of growth in the value of stock of 8·1% per annum. By way of comparison, the average rate of growth in UK Real GDP per head was less than 1% per annum over this period.

In the second instance, we must bear in mind that, if the government were to re-nationalise a utilities industry, a future government could simply sell it off again. Selling assets cheaply and buying them back dearly is no way to run a business or a nation. Even if **the UK would have been better off had it not privatised key utilities and infrastructure**, we must beware giving a future government the opportunity of repeating the mistakes of the 1980s.

Taking back control?

There is, however, another argument – that of patriotism; the spirt of "Brexit". If we want to "**Take Back Control**" of our nation, we ought to nationalise our utilities and infrastructure. Otherwise the UK's socio-economic policy will increasingly be dictated, not by Brussels, but by "**Wall Street**". Indeed, if we accept the sovereignty argument, there is a strong case for **restricting foreign ownership of the UK's key industries**, and **residential property** more generally. This is **something the EU is considering** and **other nations already do, to one extent or another**.

In sum

In short, there is a political argument for nationalisation, but probably not an economic one in general. Perhaps the answer is rather less a focus on ownership and **rather more focus on increasing democratic accountability**.