

A Survey of the Relationship between Privatization and Firm's Performance

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Abstract

Iran compared to other countries, has delay in the privatization program implementation. This led privatization plans implementation after victory of Islamic Revolution and particularly after the end of imposed war is associated with the abundant experiences of privatization programs in other countries which also using developing and developed countries experiences from performance, results, requirements, challenges and solutions perspective will have great achievement for country. One of the most important questions in privatization field is that how privatization has been successful. Many indicators used to measure the success of privatization. The present research is trying to evaluate firm's performance success and firm's performance before and after the privatization by using EVA method. To assess the impact of privatization on corporate performance, their EVA is calculating in the period of 3 years before and three years after privatization. Then by using statistical test assess their performance once a year and once a year to year and once an average of three previous years and three years after privatization. Research results shows that firm s performance in each of three periods has increasing significant growth.

Keywords: Privatization, Economic Value Added, firm's performance

1. Introduction

Today, privatization of economic reforms in many developing countries is considered as a strategic approach. Need to change the role of government, the private sector empowerment, economic competitiveness and interact with the rules of globalization and economic liberalization policies based on strengthening will necessity to the private sector. Theory of economic development actually in developed countries through the privatization leaving some of the private sector and economic has led to development in these countries. Broader conception of privatization is defined as ways to reduce the role of government and transfer it to the private sector, and following the logic of the market in all economic decisions. From this viewpoint the policy of keeping some of the activities identified by the government to prevent further development of the public sector (monopoly bleaching), decrease in the relative position of the public sector and private sector roles more points. From this viewpoint the policy of keeping some of the activities identified by the government to prevent further development of the public sector (monopoly bleaching), it points to decrease in the relative position of the public sector and more private sector roles. Entry of new private businesses can stimulate competition when the public sector has monopoly position. The government enterprises will be forced to take commercial and react to the state regulations and market forces.

The small size of government in the economy, the presence of unnecessary state-owned enterprises in economic activities, low competitiveness in the national and international economy, the lack of private sector investment in the area, weak capital market for private sector development, lack of proper distribution of resources and opportunities between the public sector and non-governmental caused after the end of the Iraq war and the first five-year development plan; since 1989, the government plans to divest part of the economic activities of state-owned enterprises to the private sector. But, privatization in organized form and based on clear and transparent rules based centralized administrative organization of the Privatization Organization; began in practice since 2001, with the implementation of the Plan development in the third quarter and also in the fourth development plan was followed as suitable supplement to mentioned law (Ghoorchian, Nadir Quli - he Zanganeh, G. 2009).

During the past decade the privatization has been an important experimental and theoretical investigation field, most developed countries have to shift to a market economy and have adopted privatization policies to improve governing company's performance (Omran, Mohammed 2009).

Nevertheless, whether privatization improves firm performance in all countries and cause GDP growth is required scientific research in this regard for each country. In the absence of comprehensive scientific research on a significant part of the privatization program during the fourth round of development (2005 to 2009 years) cause the impact of privatization on the performance of privatized firms is chosen as the subject of this study.

Privatization: the Conception

Privatization is a broad concept that has been defined in the literature of financial statements.

The Word Bank (1994): privatization is preventing the state-owned institutions and companies, and other assets are economic resources.

Fafaliou & Donaldson (2007) state that the privatization is a very broad term, but it is easy. Privatization is transfer of government services or the distribution of assets to the private sector, which can include a wide range, that sometimes prohibit the limited role of government to and sometimes provides a partnership between government and the private sector while the government is still the predominant actor.

Monari et al., (2002) believe privatization means to improve productivity and increase efficiency at the level of a country's economy is the ultimate cause economic growth.

Onyekwere (2009) argues any change in the functioning of public enterprises to private companies. Note which this definition is not includes the change in performance among parts (Such as those which occur in a quasi-government entrusted to a public company); also the most important change feature that is government desire and will not have any impact on performance of company or organization.

Savas (1992) offers different definition of privatization:

- 1) In a general definition; privatization is to meet the needs of the public private sector take a greater role than government.

2) In an operational definition; Privatization is to reduce the role of government or increasing the role of private sector in economic activity in a community or in a property of community asset (or country).

3) The third definition is the most accurate definition: transfer of state assets to private companies.

The government's role in the privatization process will be transferred to the private sector and can be divided into two main groups:

1) Providing livelihoods through: policy making, purchasing, supply and logistics, finance, law, and patent grants.

2) The second category includes activities, service activities, including the operation, the distribution of goods and services activities necessary for governance, management and sale of goods and services.

Nellis (1999) states that the privatization is ownership change so to be transferred major stock and equity of a company from public to private sector.

Hanke (1987) defined that the assignment of activities or companies that are owned or operated by government to the private sector, through sale or contract.

Rondinelli (1987): Depriving government responsibility for the administration of all or part of the activities that can be done, through the transfer these activities to the private sector or offering licenses that allow them to work as private.

Kay and Thampson (1986): words privatize are included several ways to change the relationship between government and the private sector. Including "anti-nationalization" or sale of state-owned assets, deregulation or removal of restrictive regulations and the introduction of competition in the state of absolute monopolies, contractor or transfer the goods and services produced by the government and were funded to the private sector.

Agnes Syu (1995) noted that privatization is a multidimensional concept. A conference was performed by the Scientific Committee (Ciriec), participants from different countries, presented many different definitions of privatization. For example, in the German-speaking countries (Austria and Germany), privatization was defined as transfer of ownership from the public sector to the private sector. On the other hand, French would not be considered privatization as the transfer of property rights but they insisted that they emphasis purpose of the business unit, so they emphasis on profit-oriented behavior. In this conference typically was seen the process of transferring ownership from the public sector to the private sector.

Schwartz (1989) Definition of privatization for countries with centralized economies far beyond the transfer of ownership and modifies the rules; they said: Privatization means to create a new economy's name based on markets and thus the change economic development aspects.

In this study, the concept of privatization is process of planning and implementing measures to reduce the role of government (Increasing role of the private sector) in the economic unit of society in the same way that the private sector can surpass than the public sector and the government's role less considerable than significant influence.

2. Literature review

Huang and Wang (2011) surveyed the full privatization effects of 127 companies on the Chinese stock companies. Purpose of full privatization; means transfer all shares of state-owned enterprises to the private sector. Research results shows that performance of the company after the assignment has been far better than before. Also, they found that once purchaser of private sector company were new people who had not share in the management of the company before assignment the company has greater profitability and efficiency. As well as, costs of supervision and management of the company is reduced by assignment the company to the private sector.

Vogel (2011) studied the effect of privatization on airports. They investigated the effect privatization on financial performance of airports, the performance of ten private airports in Europe by the EU from 2003 to 2009. Research results show that economic value added in ten listed companies have been mainly negative.

Meggison (2011) evaluate the effect of government ownership on the cost of corporate liabilities (the cost of debt or interest rate). They examined both the completely public and semi-public companies. On average reduction of government ownership in companies in a proportional way, thus increases the cost of obtaining credit. The results indicate that increasing the cost of debt associated with the change of ownership from public to private and this could be due to reduced government securities, risks related to new private ownership and the conflict between bondholders and shareholders of the company.

Chernykh (2011) evaluated the benefits and disadvantages of nationalization of industries in Russia they has been studied 158 of companies on the Russia stock and non-stock market during the 2004 to 2008. The results indicate that companies in this important and strategic industry while transferred to the public sector can tolerate high risk. The results also indicate that tax evasion is another factor affecting the nationalization of industries. However, little evidence was found of effective national corporate profits.

Yuce and et al. (2009) examined the effects of privatization on the performance of private enterprises in China. Sample study was consists of 4,315 firms during 1996 to 2003. The results of this research indicate that privatization has a positive effect on corporate performance. Nevertheless, the change in ownership structure will not help in the balance of power between the concentrations of ownership in the company, plays an important role. In addition, the results show that companies that combined ownership (public and private) have significantly poorer performance than state-owned enterprises, wholly private or wholly in private.

Jiang and et al., (2009) examined the effects of bank assignment to the private sector in China. After China joined, the World Trade Organization (2001) has begun to reform its banking system. This research has been conducted over 1995 to 2005 years. The results indicate that the efficiency and profitability of banks has improved after privatization.

Asefi and et al. (2008) examined the effects of privatization on productivity in Romanian companies. The results of this research indicate that privatization alone has no effect on the productivity of the company. In a competitive environment, that privatization will increase

the productivity of the company. In addition, the results indicate that company's shareholders after privatization, still the government, although has few share of the state in terms of efficiency matter when the government do not have major shareholder. The results also indicate that the privatization and restructuring are complements.

Farookhi (2012) in a study, analysis financial performance before and after the transfer of the Stock Exchange, explained the privatization process during the first quarter of Development Economic, Social and Cultural Rights in Iran determine the effect of privatization on the performance of private organizations over the past 12 years by using the market value method; Finally, the conclusion is reached that the profitability ratios, debt and leverage these organizations after privatization has improved significantly compared to the prior and only low activity was rejected also in this study, the market share of the tested after the privatization resulting in a market share increase of 15 units in the organization after privatization than before the privatization.

Nasralahi, Aghaei, Bagheri Zamani (2009) evaluated stock returns of companies privatized through the stock exchange were made in Iran during the years 1991 to 1995. In their study, were evaluated three years before and three years after the stock returns of privatization and the three subsequent three-year. In this study have been studied stock returns based on stock returns than shares, dividends per share and non-cash benefits. Research results indicate that the efficiency of privatized companies is significant differences after privatization.

Hossieni and et al. (2008) studied the effects of privatization in the Mine and Industry bank privatized companies. In this paper, were studied based on balanced scorecard model, indicators and evaluation criteria of the four corporate financial perspectives, customer / market, internal processes and learning and growth companies, before and after transfer by using TOPSIS techniques. This study represents the result that although the assignment some companies has been positive but however, if not properly controlled by the transfer and continuation of the existing situation, many of these companies in the near future the situation will be worse and returning to the Bank.

Almasi (2002) were examined privatization of state economic development programs in the framework of the financial perspectives. Evaluate the effectiveness of these policies and privatization of the accounting literature using three benchmark earnings per share and return on equity returns on assets. The three criteria listed in the five years before and five years after privatization in various industries such assessments. The results show that the financial performance of privatized firms is not significantly changed. The privatization policies to achieve its goals improved efficiency and productivity. Main cause was bad economic situation and the lack of appropriate to achieve objectives of the program.

3. Research Hypothesis

This study sought to compare the performance of the company before its privatization. The performance of the company through the economic value compared before and after the privatization and the indicators have been considered as independent variables. In order to test the following hypotheses are postulated.

H_0 : Firm performance after privatization has a significant difference than before.

H_1 : Firm performance after privatization has not significant difference than before.

Variables of the study

Economic Value Added

Economic Value Added defined as net operating profit after deducted the tax from the cost of capital. Cost of capital is including all finance expenses such as loan interest and equity expected return. All the mentioned cost manifested in the average cost of capital. The general formula for calculating the economic value is as follows. (Richard S. Warr, 2005)

$$EVA = NOPAT_t - (WACC * Capital_t - 1)$$

EVA: Economic Value Added

NOPAT t: Net Operating Profit after Tax at the end of t period

WACC: Weighted Average Cost of Capital rate

Capital t – 1: Total of capital to book value at the beginning of t period (end of t-1)

Calculating the Net Operating Profit after Tax according to the operational approach as indicated in below table.

NOPAT	
Net sale	*****
Cost of sold goods	(*****)
Operational Cost	<u>(*****)</u>
Operational Profit	*****
Other cost or revenue	*****
Increase in capital equivalent	*****
Tax	<u>(*****)</u>
Net Operating Profit after Tax	<u>*****</u>

Increase in capital equivalent is include increasing in depreciation reserves inventory, increase in depreciation reserve investments, increase in doubtful receivables storage, increase in supply and an increase in deferred costs of employee termination benefits service (Talebi, 2003).

In addition, to calculate the Net Operating Profit after Tax (NOPAT), tax will be calculated as follows:

$$Tax = Operational\ profit * Effective\ tax\ rate$$

Effective tax rate considering Iranian's direct taxation law and is intended according to ten percent listed companies in Tehran Stock Exchange tax breaks. Based on this effective tax rate is 22/5% (Davani, 2007).

To calculating cost of capital rate using the Weighted Average Cost of Capital rate (WACC) that is calculated as follow:

$$WACC = (W_e \times K_e) + (W_d \times K_d)$$

Where:

W_d = debt weight

W_e = equity weight

K_d = Cost of debt rate

K_e = Rate of common equity cost

Calculation the cost of each source of financing rates method is as follows:

A) Cost of debt rate (K_d):

The cost of debt is calculated as follow:

Cost of debt is part of capital cost that is pay for provide the out of entity fund. In fact this cost is consisting of interest that is paid for interest-bearing liabilities, such as short-term and long-term debt. In the case of companies that have issued bonds, it is added to the cost of the bonds. Given the number of loans received by the company, it's considered a simple average of the costs and debts. According to studies, the simple average interest facilities rate during the study period is considered 18 percent.

B) Cost of common stock rate, retained earnings and reserves (k_e):

In order to calculate the cost of common stock rate, retained earnings and reserves use discounted cash flows (DCF) method or ... model that is described as follow:

$$K_e = \frac{D_0(1 + g)}{P_0} + g$$

Where:

D_0 = Cash earnings of per share in the current period

P_0 = Per stock price

g = Dividend growth rate

Calculate the weight of each source of financing is as follows:

Weight of each source is obtained from divided the market value of each source to the total employed market value of resources. According to the debt total market that is approximately equal to their book value, thus considered the book value.

Total source = value of common stock market + Book value of interest bearing debt

Based on weight of each source is calculated as follow:

Weight of interest bearing debt = (K_d)	Book value of interest bearing debt
	Total market value source
Weight of common stock = Retained earnings and reserves (K_e)	value of common stock market
	Total market value source

Research Methodology

This type of research is after the event. In this study, the aim is to examine the relationships between variables and data on the natural environment in normal way or past events that have occurred without the direct involvement of researchers, to collect and analyze.

Statistical community and Sample

In this research statistical community is collection of listed companies in Tehran Stock Exchange that somehow occurred whole or in part privatized during the study period (2004 to 2008). Thus, researcher has intended specific requirements that meet the conditions necessary for statistical studies. The mentioned conditions are as follows:

1) Privatization of the company is subject to the definition contained in this research study period (2004 to 2008).

2) Financial information required is fully provided to performing this study for three years before and three years after privatization.

3) During the years following the privatization the companies is not affected by temporary or permanent suspension. It should be noted that this cessation includes regular stops are not associated with holding annual general meetings and extraordinary communities of company.

4) Year of privatization has not been considered as a year of change in performance criterion analysis in this research. With the above explanation of the used sampling method in this study but is selected elimination method between the statistical population. In relation to the all performed privatization of the mentioned period, 309 companies that number 169 of them is not part of stock companies, thus has been removed from statistical population and 141 member companies belong to the stock exchange or with transfer of the Stock Exchange, are members of the Stock Exchange. From these 107 assignment cases is not included in the privatization definition (Government is only little shareholder of the company and a small portion of the stock is assigned) and are eliminated from statistical population, so statistical population of this research is consist of 34 privatized companies. It should be noted that according to the below table, during the course of researching assigned share value has through the Stock Exchange.

Figures in U.S.1000 \$

Supply method	2004	2005	2006	2007	2008	Total without 2004	Percent
Stock Exchange	Disaggregated data was not available	50,110	2,688,503	17,405,556	20,154,140	40,298,309	78
Negotiation		0	0	0	0	0	0
Auction		34,402	65,292	9,325,668	2,096,273	11,521,635	22
Total	85011	84,512	2,753,795	26,731,224	22,250,413	51,819,944	100

Data collection

In order to data collection and research literature in the fields of theoretical background and information about the company is using the following methods:

- * Study Persian and Latin books, articles, dissertations research conducted related to the topic.

- * Information bank of listed companies in Tehran Stock Exchange.

- * ... and ... software.

After gathering the data by Excel and Access software summarizing, coding and classification, finally has been analyzed by using the statistical SPSS software package.

Research Hypothesis Test

Conducted to study the changes of privatization, the Economic Value Added of private companies was extracted 3 years before and 3 years after privatization. Then according to data normalization has been chosen. This test is used for significant differences compared to the average performance of the company over several years.

Wilcoxon Test

Wilcoxon Test is applied when the researcher is going to depend on two different amounts of qualitative data in this study. This test considers the size difference between the ranks. Thus variables can have different answers or either distance. This test is corresponding with dependent two-sample t-test and considering and if there is no t-test conditions is good substitute for it. Samples are used in this test must be matched (paired) to the rest of their attributes. To calculate test criteria first obtained difference between the paired data (first - second) then sorted the subtraction of paired according to their absolute. Withdrawn zero difference and if difference of several items are identical assigned to each one occupy both mean rank. To obtain rank test criteria sum that criteria related to positive observations.

Friedman Test

Friedman test is for prioritizing and ranking the most influential variable on the dependent variable. This test was complete randomized for block design that has been named for its famous economist inventor Milton Friedman; in fact, Friedman test generalization of the sign test means for the two treatments, Friedman test, is equivalent to the sign test. Friedman test is compare several groups according to their average rank and determine whether these groups may be one community or not? This test should be at least a rating scale. In addition, Friedman test is used through rating for two-way analysis of variance (for non-parametric data), and to comparison ratings for different groups. The number of samples should be the same that consider as disadvantages of this test. All samples should be matched. In other words, this test is used for testing the hypotheses that is derived from several measurements. Friedman test to calculate the values of the dependent variables are sorted and then compare to the average ranks.

Research Limitations

Following limitations exist in the study that may affect the results:

- 1- Due to changes in the general level of prices in Iran, part of performance results may be related to the topic that is not considered in this study.
- 2- Iran's economic situation may do not provide be the governmental economic policies about determination sales prices in competition environment for private companies.

Research results

To test data normality first of all by using the test, evaluate data normality. The results of these tests are presented in the below table.

	First year	Second year	Third year	Fourth year	Fifth year	Sixth year	Seventh year
Z	1.554	1.468	1.270	1.191	.954	1.021	.879
Sig	.016	.027	.079	.117	.323	.248	.423

Test results in different years were different. Test results of the first and second years at 5% significance level was not representative of normality in the selected sample. Also, to determine statistical test for comparing the three years before and three years after privatization, using ... test to test all 3 years data that results are presented in below table.

	Average of three years before privatization	Average of three years after privatization
Z	1.514	.802
Sig	.020	.540

The results indicate that the sample data are normally three years after privatization while are not normal in the three years prior to privatization. Due to the lack of statistical normality, use the nonparametric ... and ... test to comparison their means. Performance compared to the previous three years and three years after privatization, as can be seen in the table above; the average of economic value added has so many differences between

before and after privatization that ... test the as following table describes will confirm significant difference between at significance level of 5%.

Z	-2.146a
Sig	.032
Average before privatization	31.712
Average after privatization	173.215

Performance results, compared with the years before privatization years after the privatization year is presented in the table below. As can be seen in this table, while approaching the fourth years of privatization, generally economic value is increasing that cause to create meaningful difference between years.

Average ratings	First year	Second year	Third year	Fourth year	Fifth year	Sixth year	Seventh year
	3.41	3.18	3.50	3.78	4.63	4.62	4.88

To evaluate the significant difference between the economic values added in different years was used Friedman test. Estimation results of this test are as follows:

No.	34
Chi-Statistic	21.058
Freedom degree	6
Sig	.002

As mentioned in the above table, Friedman test at a significance level of 5%, confirms there are significant differences between different years before with years after privatization.

Conclusion

Finding a way to improve economic condition is one of the biggest concerns of every state in the completely wide world. Among the problems that many governments, are facing especially in less developed countries bulk of the government and the extent of its involvement in many unnecessary activities that cause increasing in costs, loss of productivity and efficiency, establishment of parallel institutions and the lack of management power. This has led to an effective solution to this problem, have thought politicians and economists. The concept of privatization as one of the basic strategies have been proposed to solve this problem in this context, privatization is applicable to different ways, therefore in this regard perform a variety of different privatization methods, is provide a wide field of study and investigation. One of the most important issues in the research is to examine the firm's performance before and after privatization.

In this research by using EVA method, examined the firms performance before and after privatization. To evaluate this matter performance of companies were examined by using economic value in the three-year period before and after privatization, and using ... and ... test. The results of these tests indicate that each of the company's performance in the three-year period before and after privatization has significant meaning. In other words, the privatization of these companies has cause in an economic value added growth.

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