

PRIVATISATION AND ITS
IMPACT ON PRODUCTIVITY

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Privatisation and its Impact on Productivity

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DEDICATED TO MY BELOVED PARENTS

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ
الْحَمْدُ لِلَّهِ رَبِّ الْعَالَمِينَ الرَّحْمَنِ الرَّحِيمِ
مَلِكِ يَوْمِ الدِّينِ إِيَّاكَ نَعْبُدُ وَإِيَّاكَ نَسْتَعِينُ
أَهْدِنَا الصِّرَاطَ الْمُسْتَقِيمَ صِرَاطَ الَّذِينَ
أَنْعَمْتَ عَلَيْهِمْ غَيْرِ الْمَغْضُوبِ عَلَيْهِمْ
وَلَا الضَّالِّينَ

اللَّهُمَّ صَلِّ عَلَى
سَيِّدِ رُسُلِكَ وَخَاتَمِ أَنْبِيَائِكَ
مُحَمَّدٍ وَآلِهِ الطَّيِّبِينَ الطَّاهِرِينَ
وَصَلِّ عَلَى جَمِيعِ الْأَنْبِيَاءِ وَالرُّسُلِينَ

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CHAPTER I

INTRODUCTION

The new trend towards government involvement in the economy has been seriously questioned. Indeed there have been attempts to rely more heavily on deregulated free markets for the allocation of resources. In particular, there has been a significant move toward privatisation and the private provision of public infrastructure and services.

Privatisation i.e. the transfer of government assets or function to the private sector is a phenomenon that has been growing rapidly around the world. In the United States, private firms in thousands of cities provide ambulance services, garbage collection, street repairs, recordkeeping, and many other services. In Canada, the government is taking steps to sell shares in the state-owned airline. Mexico has sold dozens of nationalized companies to the private sector and has over 200 state firms scheduled for sale.

Several Asia countries are also turning to privatisation. Not only have Indonesia, Malaysia and Thailand introduced this concept, but so have Singapore and Taiwan which are the private examples of successful development states. Similar interest is also being shown in India, Bangladesh, Sri Lanka and Pakistan.

In Europe, Turkey, France and the Federal Republic of Germany have also set the process in motion. But it is Britain that leads the world in privatisation. In that country, asset sales have become a major government strategy to deal with the basic economic problems.

Since independence Malaysia has interchangeably introduced various policies pertaining to the development of the country.

Beginning with the introduction of the New Economic Policy, the role of government has risen to become the driving force in motivating the country towards achieving the goals and objectives of the Malaysian economy.

However, the phenomenon of government involvement paused after the new policy of privatisation and its complementary Malaysia Incorporated has been introduced announced by the Malaysia Prime Minister Dato Seri Dr. Mahathir Mohamad in mid - 1982. In his words, the Prime Minister said, "government the world are notorious for inefficiency when running enterprises, even when aided by monopoly and the authority of government. On the other hand, the private sector is better motivated and generally more efficient. It is hoped that privatisation will improve the economy and general performance of the services, resulting in a more rapid growth of the nation as a whole".¹

The need for the reversal of the government policies has recognised various limitation in development strategies. Hence, privatisation represents the trusts of new development strategy for Malaysian in the decade of eighties onwards. There are number of reasons which can be given proper measure in order to understand why privatisation is inevitably introduced.

It has been shown that government-owned and managed business are not necessarily good for the workers. In communist countries the workers remain poor while money is spent on arms, power games and proxy wars. In socialist countries the most striking thing is the number of strikes and demand for better treatment by workers in

¹The speech in opening the national conference on the security industry in Malaysia, April 1984.

government-owned industry. Obviously, government ownership does not necessarily mean absence of exploitation.

At the same time public owned enterprises never seems to be profitable or efficient. Even when they are monopolised they cannot seem to earn their way much less pay tax or dividends to the government. More often than not, a privately owned enterprise which has been making profit and paying taxes, not only ceases to do both on nationalisation but require subsidies and copious injections of capital every now and then by government.

Briefly, there are several important and critical reasons for the adoption of privatisation policy by the Malaysian government.

- a. The size of the public sector has increased tremendously which consequently, worsen its financial burden and deficit. Public sector expenditure as proportion of GNP grew from 28 percent in 1975 to about 36 percent in 1982.
- b. Government enterprises have not been handle efficiently, thus, privatisation is a way out for the public sector to improve activities and productivity in most areas.
- c. The available financial resources create difficulties for government to continue maintaining and providing free or subsidized services that the public demand.
- d. The competitive environment prevailing in the private sector is expected to improve quality of services and enterprises that will be privatised.
- e. To increase opportunities for ownership participation

of Bumiputra and other Malaysian.

f. The adverse repercussion of recession.

In effect, the introduction of the privatisation policy reflects the change in development strategy from statism to private capitalism resulting from the need for economic growth and expansion, efficiency and higher productivity.

In view of the Malaysian context, at the moment, privatisation is regarded as the best alternatives of development strategy. Nonetheless, the political-economic dimension should also be given proper consideration. There are many questions to be answered pertaining to political economy.

For instance, why is it that after more than ten years of government involvement in providing social services that it has advocated and, in some instances, set about reducing the role of state? What was privatisation intended to achieve? What are the implication of this policy? In short, what is the political economy of privatisation?

In order to answer this questions, one has to really understand the situation underlying the countries itself. In Malaysia, the development is rife with issues pertaining to inequalities and imbalances. Economic-ethnic disparities rural-urban imbalances, regional differences, vertical inequalities urged the questions, who will gain and who will benefit? And who will bear the cost of privatisation? To what extent will privatisation result in perpetuating of the whole range of socio-economic disparities in the country.

Privatisation is aimed at modernising the Malaysia economy. This will have to take place within a specific natural framework, particularly within the New Economic Policy (NEP) which is geared

towards eradicating poverty, restructuring ownership and employment in a comprehensive attempt to upgrade the quality of life of Malaysians.

1.1 Purpose and Significance

Privatisation policy has been debated lately about its pros and cons. Strong points have been raised by the proponents and opponents of privatisation as a development strategy in Malaysia.

The main purpose is to focus on the impact of the privatisation policy introduced in Malaysia. How far does it suit the economics, political and social need of the country. Hence this study will anticipate the effects and implication of the privatisation policy and help to clear some of the fears and doubts that have been raised, despite the good intention. More specifically, it will help to chart the course of Malaysia development for the future.

On top of that, this study will also try to analyse and evaluate the concept of privatisation from the Islamic viewpoint. This humble attempt is not just for the sake of viewing but it is hope that it can contribute something towards the achievements of the development goals.

1.2 Objectives of Study

The objectives of study are broadly outline as follows;

- a. To study the concept, approach and method of

privatisation.

- b. To investigate the relationship between the public and the private sectors in term of:
 - i. the role of government or state - In this context the questions that are critical to analyse are - what activities should the government be responsible for?, to what extent should it be involved in the selected activities.
- c. To analyse the impact of privatisation on greater productivity in term of;
 - i. effects on the government's role
 - ii. effects on the management and employees
 - iii. identification of the sources and investment for privatisation and the effect on employers.
- d. To see how Islam views on privatisation which can be observed from two angles;
 - i. ownership in Islam
 - ii. the role of Islamic State.

1.3 Outline of the paper

The writer attempts to present the issues with regard to the development strategies. Hence, in this paper, the impact of privatisation will be stressed in view of the Malaysian context.

To achieve this objective, the writer has divided the paper into seven chapters altogether. Chapter I begins with this chapter. This introduction chapter will give the overview of the subjects which will be discussed in the whole chapters.

Chapter 2 concerned with the methodology of the paper. This brief chapter touched on the method of analysis undertaken and some of the problems and limitation encountered.

Chapter 3 focussed on the review of literature. The important points of the paper will be highlighted by referring to books and articles related to the subject.

The overview of Malaysian Economy is discussed in chapter 4. This will include the trend of the development in Malaysia which led to the implementation of privatisation policy.

In chapter 5, the impact of privatisation is thoroughly discussed. Since this is the main chapter, major parts of it were diagnosed indepth.

Chapter 6 focussed on the issues of privatisation from the Islamic perspective. The writer attempts to identify the subject of privatisation which related to Islam. This led to the discussion on the Islamic concept of privatisation.

The final chapter is concluded by some suggestions from the writer. It is hope that this study will help the reader to understand further on the subject of

privatisation particularly looking from the Islamic viewpoint.

CHAPTER II

RESEARCH METHODOLOGY

The study is an attempt to analyse and investigate the impact of privatisation on greater productivity. The focus will be on the question of whether or not privatisation brings impact on greater productivity.

In this chapter the writer will briefly examine the methods to be used and the limitation encountered. During the course of study great emphasis will be put on the Malaysian economy.

2.1 Library Research

This method of study has been chosen because apart from the only suitable alternatives it is the most suitable way of getting the data pertaining to the subject. The reasons why the other methods were not chosen will be discussed under the limitation of the study.

There have been a number of qualitative materials such as books, journals, newspapers, magazines and periodical articles discussing on the subject of privatisation. Currently in Malaysia, there have been a serious discussion on privatisation policy by the government.

Subsequently, there were many forum and seminars organised to discuss on the subject and hence many books edited and published materials were in the market. There were also many articles and journals which can be found discussing on the subject. This qualitative

materials enable the writer to acquire informations and to enhance the study on privatisation.

2.2 Discussion

This method undertaken by the writer in order to better the understanding on the subject of privatisation. The discussion were made with the lecturers and the people involved in the implementation of privatisation in Malaysia.

2.3 Limitation of the study

Obviously there will be problems to encountered in this study since privatisation is still a new government policy. In Malaysia, privatisation only started four years ago and thus, very few data were gathered. Due to this fact, the writer will only discuss on this subject theoretically by using the secondary sources. The short comings of the study are as follows:

2.3.1 Lack of relevant data

There were scarcity of data to be used in the study. This is due to the fact that privatisation is still a new area of study. Furthermore, there were only little data gathered by the authority or individuals which can be made a reference for the study. The authority on the other hand, has put little effort in getting the data for information. Hence, it is difficult to investigate exactly the impact of privatisation on productivity.

2.3.2 Paucity of published materials

There were not many published materials discussing on privatisation in the market. The insufficiency of published materials has made the inquiries more cumbersome. There were only few books edited and articles discussed on privatisation which are relevant in the study. Even though there were many journals discussing on the subject but most of them were irrelevant in the Malaysian context.

2.3.3 Lack of quantitative materials

There were hardly or no quantitative materials which can be cited in the secondary sources relevant to the study. The quantitative materials or empirical investigation is important in enhancing the understanding of some well-established theory.

CHAPTER III

REVIEW OF LITERATURE

Privatisation in actual fact is not a new concept or policy which have been undertaken by many countries in the world today. It is infact existed more than 200 years ago where economist Adam Smith advocated privatisation as a means of eliminating waste and maximizing the value of assets.¹

However, today the concept of privatisation has been further modified according to the needs and interests of the countries. In this paper the writer attempts to venture in the areas where privatisation is asserted to have an impact on the economy.

The main question to be focussed here that whether privatisation has an impact on greater productivity. Hence, the review of literature shall covers only one main aspect of privatisation i.e. its impact on productivity.

3.1 Impact on Productivity

One of the reasons for privatisation is that it can generate productivity. According to Lee Siang Sun,² the public sector has been involved actively in the commercial activities and as such, the size of government has grown tremendously. Such growth has a heavy burden on the government finance. In addition,

¹Steve H. Hanke, "The Privatisation Option: An Analysis", in Economic Impact, vol, No, 55, (1985), p. 16

²Lee Siang Chin, 'Privatisation and its impact on greater productivity', paper presented at a Symposium on "Strategies Towards Higher Productivity", Fakulti Ekonomi Dan Pentadbiran, Business Management Alumni, Kuala Lumpur, 1981, p. 2

it also burden on the government to reduce its role through privatisation.

Another major reason is that government wishes to streamline and improve the efficiency of the public service. When self-sustained government departments and viable government corporations can be privatised, it will result in improvement in productivity in most areas such as service, financial returns, more efficient work force, higher taxes for government and improved working environment for the employees.³

Tengku Ahmad Rithauddin⁴ stated that the rationale for privatisation lies in the need for cooperation between the government and the private sector for increased productivity. Government ventures in commerce and industry have in many instances been unsuccessful partly due to the differences between government culture as opposite to business culture. Hence, there is a need to hand over to the private sector activities that it can manage efficiently. With less government-private competition, there will develop better government and business cooperation for increased productivity and industrial growth.⁵

³Ibid., p. 3

⁴Tengku Ahmad Rithauddin, "Privatisation and National Productivity in Commerce and Industry," M. Nor Chani, I.K.M. Chia, B. Gale (Eds), Malaysia Incorporated and Privatisation Towards National Unity, 1984

⁵Ibid., p. 22

Cooperation between the public sector and private sector is significant but insufficient without the fast and efficient decision - making by the management level. Mohd. Nor Abdul Ghani⁶ elaborates productivity of the nation ultimately rest on the productivity of management, both in private and public sectors. It is the responsibility of private and public sectors to get things moving by having a fast decision - making from the top level to the bottom level. A failure or delay in the decision - making process by the decision maker will cause a low productivity or under - utilization of work capacity in any organizations.

Privatisation in Bernard's⁷ opinion is not the end on the only objective. It is just a means to an end. The end must necessarily be the increase of national productivity on one hand and the reduction of public expenditure on the other.

The objective of the nationalized industries are prescribed in the most general forms and the role of nationalized industry managers as that of trustees of public interest.⁸ Hotelling prescribed the pricing and

⁶M. Nor Ghani, "Management and Decision - Making and Productivity," in Dr. B.T.H. Wang, Dr. I.K.M. Chin, B. Gale (Eds), Malaysia Incorporated and Privatisation Towards National Unity, 1984.

⁷B.T.H. Wang, "The Need for Discussion and Evaluation", in M. Nor Ghani, I.K.M. Chin, B. Gale (Eds), Malaysia Incorporated and Privatisation Towards National Unity, 1984.

⁸J.A. Kay and D.J. Thompson, "Privatisation: A Policy in Search of Rationale," in The Economic Journal, p. 20

investment criteria which such trustees would wish to follow.⁹ An early and perceptive critic of the hotelling was Little,¹⁰ who was concerned by its neglect of appropriate incentive to productivity efficiency.

J.A. Kay and D.J. Thompson¹¹ stated that privatisation concerned with incentives to both productive and collective efficiency. Productive efficiency requires that whatever is done should be achieved at minimum cost; allocative efficiency implies that what is done meets consumer needs at prices which reflect the cost of provision.

They further stressed that privatisation tends to promote productive and allocative efficiency. The incentive to productive efficiency comes from the requirement on private firms to achieve profits - to stay in business in competitive product markets, to avert the threat of takeover from the 'the market for corporate control'.

Chong Tsu Mun,¹² clarifies that in the process of privatisation, job opportunity is increased despite the decline in the unemployment rate. Division of work and

⁹Hotelling, H. (1938), 'The general welfare in relation to problem of taxation and of railway and utility rates', *Econometrica*, as cited in J.A. Kay and D.J. Thompson, "Privatisation: A Policy in search of Rationale," in *The Economic Journal*, p. 20

¹⁰Little, J.M.D. (1952), "A critic of welfare economics," Oxford; Oxford University Press, as cited in J.A. Kay And D.J. Thompson, p. 20.

¹¹J.A. Kay and D.J. Thompson, op. cit. p. 20

¹²Chong Tsu Mun, "Pengswastaan Agensi Awam Tingkatkan Kecekapan Berkhidmat", Utusan Malaysia, 30 April 1986, p. 8

time according to the skills is created to acquire higher productivity. This will lead to increase in the national income and lessen the government's burden and hence, government debt will be settled as soon as possible. In the long-run when private sectors becoming more experience and more skillful, efficient and effective, and able to achieve economics of scale, the productivity will be increased. C.T. Mun added further, that with the existence of privatisation, the competition between the public and the private sector will be lessen in order for productivity to increase.

Steve H. Hanke¹³ proved by giving evidence of the impact of privatisation on productivity. According to Steve, although economic theory as well as common sense, strongly support the notion that private enterprises should be more efficient and productive than public enterprises, one question remained unanswered; Does the evidence support theory?

Steve gave the evidence to support this theory by asserting that in the USA, Federal productivity is lower than productivity in the private sector. Consequently the unit labor cost levels, for similar types of output, are typically higher in the Federal sector than in the private sector.

¹³ Steve H. Hanke, "Privatisation : Theory, Evidence and Implementation".

Deregulation is one form of privatisation. Economic deregulation is the first major victory of free market economy in American public policy and it sets an important precedent. By liberating price controls and permitting competition, the deregulation revolution has allowed entrepreneurs to find the most profitable ways of serving customers. The result of this deregulation is to lower prices, improve customer service and choice, hasten technological change in the previously cartelized, and bolster the competitiveness and efficiency of the American economy as a whole.¹⁴

Robert Okun further discussed that the industries experiencing this deregulation have substantially improved. Labor productivity has soared, particularly in transportation, as downward cost pressures have focussed changes in inefficient rules and inflexible labor contracts.

Dire predictions that cost would rise after deregulation have been refuted in industry after industry. Okun described¹⁵ between 1980 and 1985, 76 major new carriers and 203 commuters liners entered industry. The result was more competition than ever before and finally boosting worker productivity.

¹⁴B. Robert Okun, "The Benefits of Deregulation", in Economic Impact, Vol. No. 55, (1985/3), p/ 26

¹⁵Ibid., p. 27