

The background of the slide features a large, semi-transparent watermark of the Northwestern University seal. The seal is circular and contains the text "ORTHWESTERN UNIVERSITY" around the top edge and "1859" at the bottom. In the center, there is a book with the Greek text "ὁ λόγος καὶ πλήρης ἀληθείας χάριτος θείας" (The Word and full of truth, grace and divine gifts) written on it.

Take the Money and Run? Privatization and Rent Extraction

Felipe Gonzalez, Mounu Prem, Francisco Urzua

Paola Sapienza
Northwestern University

Summary (with my own lenses)

- Privatization under Pinochet, two outcomes:
 - Non corrupt privatization
 - Corrupt privatization(no observable difference, but industry differences?)
- Describe differences
- Focus on post regime changes
- Very interesting paper in light of “Chicago boys” recommendations.

What are the consequences?

- “Corrupt” privatized firms are larger at the end of the dictatorship and receive more loans from state-owned banks
- After the dictatorship ends:
 - Stock market performance drops (market prices the loss of political influence)
 - **Yet**, these firms “recycle” themselves and form new political connections (maybe not so effectively?)
 - Pyramidal structures are formed
 - Persistence of devious behavior after regime change (illegal political contributions, hiring politicians for board seats...)
- Is this just persistence in behavior, or is it optimal from a political economy perspective? What is the role of democratic leaders in the paper?

My recommendation: we can learn more

- Frame within theory.
- The topic is persistency of institutions/behaviors/norms when transitioning from dictatorship to democracy
- Lack of a mechanism that explains the persistency
- Resource curse literature and institution building
- The paper can effectively speak about the transition from repressive leaderships controlling crucial resources to democracy. What does need to happen for the resource curse not to be present after regime change? Why persistency?

Industries are not random

Industries: energy production and distribution, telecommunication, and extraction of mineral

Can industry give us a window into the mechanism during transition?

1) What Pinochet wanted to control most. Telecommunications & natural resources (typical for dictators, see Guriev, Kolotilin, and Sonin, 2006).

2) What Chicago boys wanted to privatize the least . Energy and telecommunications. In the 70s most countries had no experience in deregulation of the energy sector. Things could go wrong.

3) Corporate governance / managerial incentives story. Some industries are mine and sell (e.g. coal or minerals in the case of Chile). Some industries need to produce products that are competitive on the international markets, you need good management. Evidence shows that resource limited dictatorships (Southeast Asia) allow the private sector to grow, while resource-rich dictators milk the resource sector crowding other industries to take off (Egorov, Guriev, and Sonin (APSR 2009). Bad managerial habits persists in democracy.

4) Resource curse theory. Rents transferred from the potentially efficient primary sector into non-tradeable sector that includes slow-maturing infant industry and non-productive public sector employment. This maintain political power if there are enough resources. What happens in democracy transition then?

Theory – my intuition

Adapt from Caselli (2006), Robinson and Torvick (2006), Egorov, Guriev, and Sonin (2009).

Elites decide how to allocate the revenue between its own enrichment, activities that increase the elite's chances of retaining power, and investments that can increase the economy's capacity to produce non-resource income.

- If there are binding budgets, when the return from staying in power increases, leaders substitute away from productive activities (resource curse) / even w/o binding constraints with negative spillovers between industries.
- The stronger the control over resources of the leader, the higher the probability of facing a challenge ending his control. The leader could either extract more or improve sharing with others to stay in power.

What happen when dictator is ousted from power? what is the optimal response of challengers? Use the resource curse literature to understand transition to democracy. This would be the first paper to do this.