WORLD BANK AND THE CASE FOR PRIVATISATION

Development in Peru in the 1990s

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Maailmanpankki on vaikutusvaltaisin kehityspoliittinen toimija. Tutkimuksen tarkoituksena on selvittää Maailmanpankin rakennesopeutusohjelman yhden osan, yksityistämisen, vaikutuksia kehitykseen Perussa. Peru kävi läpi laajan ja nopean yksityistämisprosessin 1990-luvulla Maailmanpankin neuvojen mukaisesti. Tutkimuksen aineistona on lähinnä Maailmanpankin omat tilastot ja tutkimukset Perun yksityistämis- ja kehitysprosesseista.

Ensin käyn lyhyesti läpi Maailmanpankin historiaa ja kehitysajattelua, sekä tapaa mitata kehitystä. Erityisesti keskityn Maailmanpankin tärkeimpään tehtävään 1990-luvulla: köyhyyden vähentämiseen. Tämän jälkeen luvussa kolme tarkastelen Maailmanpankin teoriaa yksityistämisestä, ja siitä kuinka yksityistäminen edesauttaa maan kehitystä. Maailmanpankin mukaan yksityistäminen nopeuttaa maan taloudellista kasvua ja tätä kautta vähentää köyhyyttä. Lisäksi yksityinen sektori toimii julkista tehokkaammin, joten tuotteet ja palvelut ovat edullisempia ja paremmin saatavilla, myös köyhille. Maailmanpankin mukaan yksityistäminen myös poistaa mahdollisuuksia lahjontaan ja korruptioon sekä tuottaa lisää työpaikkoja.

Lopuksi käsittelen yksityistämisprosessia Perussa 1990-luvulla ja sen vaikutuksia kehityksen eri osa-alueisiin. Yksityistämisen seurauksena yksityistettyjen yritysten tuhannet työntekijät menettivät työnsä, mutta arvioiden mukaan työllisyystilanne kuitenkin parani alihankintojen ansiosta. Vaikutus korruptioon on vaikeampi todentaa, mutta korruptio oli läpi 1990-luvun suuri ongelma Perussa. Yksityistämisen vaikutus taloudelliseen kehitykseen on ollut suotuisa, mutta taloudellisesta kasvusta huolimatta köyhyys ei ole laskenut. Koska talouden kasvaessa myös eriarvoisuus on kasvanut, voidaan päätellä, että yksityistämisestä tulleet hyödyt ovat jakautuneet epätasaisesti yhteiskunnassa. Tämän vuoksi köyhyys, Maailmanpankin tärkein kehitysmittari, ei ole laskenut.

Kehityksen monimutkaisuudesta ja monimuotoisuudesta johtuen, yksinkertaista vastausta kysymykseen ‘onko yksityistäminen parantanut kehitystä?’, on vaikea löytää. Loppuluvussa käsittelen lyhyesti myös erilaisia kehityksen määritelmiä, joissa taloudellisilla tai muilla mitattavilla ominaisuuksilla on pienempi merkitys kuin ihmisten elämän laadulla, onnellisuudella, vapaudella ja itsenäisyydellä.

Avainsanat: World Bank, privatisation, Peru, development, structural adjustment programs, poverty

CONTENTS

1. INTRODUCTION

Economists, social scientists and other scholars have studied problems of development for decades. Various theories have been made and policies formed in search for the answer to development problems. Despite many successes and positive changes, it still seems that many developing countries and their citizens are poor and unable to better their situation. I find the question of poverty in the world of overwhelming prosperity very interesting, and therefore decided to write my thesis on problems and opportunities of development.

The World Bank is the single most influential actor in development field and is therefore an object of my study. Projects and loans of the World Bank have been widely criticised from the left and the right, by environmentalists, academics and grass root organisations. Despite wide criticism, the Bank has also numerous supporters. After over 50 years of work in the development field, the Bank continues and expands its programs and projects, and is supported and financed by numerous governments, both in developing and developed countries. Perhaps the most criticised of all the Bank actions have been the structural adjustment programs (SAPs). In the early 1980s, the SAPs were a new form of lending. They were initially a response to the debt crisis in developing countries. The SAP loans were not given to development projects like the previous development loans, but for governments which would change their policies according to the recommendations of the World Bank and International Monetary Fund (IMF). The SAP's were designed to cut government expenditure, reduce the state intervention in the economy and to promote liberalisation and international trade[1].

My initial idea was to study how the policies recommended by the World Bank in SAPs have affected the development of one country where they were implemented in the 1990s, Peru. I wanted to choose just one country in order to avoid the biased view of many writings. In my view, the critics of the Bank tend to choose examples of the Bank failure from numerous countries in their writings, and then argue that the policies do not work. And the Bank and its supporters choose positive examples and argue the opposite. I wanted to be able to find both positive and negative effects.

It soon became clear that studying the effects of all the adjustment measures, which include export promotion, downsizing the civil services, economic liberalisation, tax reductions and privatisation[2], would be far too wide area to study. Therefore I decided to narrow it down and choose just one of the SAP policies and examine what consequences it had on development in Peru. The SAP policies are of course intertwined in many ways, supporting each other and it is sometimes not easy to see if the consequences are more from one policy or another. SAP policies were, and most of them still are, the ways in which the Bank believes a country can triumph in development. SAPs were the Bank's ideal development paths in the 1980s and 1990s.

There were many reasons why privatisation seemed the best research area. Of the SAPs, privatisation was the one most thoroughly followed by Peruvian government. The reason why I chose Peru as the object of my research was my interest in the history of Latin America. Latin America is not as poor as Africa, and most countries in Latin America are considered as middle-income countries. Peru is usually categorised as a 'lower middle-income country'. Interesting in the Latin American countries is their highly unequal social structure. Peru turned out to be a good choice, because of its rapid turn from 'unorthodox' economic policies in the 1980s to World Bank advocated 'orthodox' policies in the 1990s. Peru began privatisation in 1991, and therefore my research on the impact of privatisation is focused on the 1990s. Privatisation is still a very current topic and raises debate in developed as well as in developing countries. Privatisation is connected to many development themes, such as the role of the state and private sector in development, to the debt question, poverty, and to the allocation of resources and services.

My aim is to compare the World Bank theories for privatisation to empirical evidence of consequences of privatisation in Peru. Object of my study is the World Bank's development idea in the 1990s, where privatisation was considered beneficial and even mandatory for development. I am interested in finding out, has the privatisation developed Peru, or has it done more harm than good as the critics claim. From the data I have collected, I will examine has there been such favourable consequences as the Bank has anticipated or have the critics of privatisation been more accurate. My primary

[1] Simon, David (2002), 87
[2] Simon, David (2002), 88

sources on privatisation and development in Peru are the World Bank publications and web-site, especially World Bank's Country Assistance Strategies (CAS) for Peru in 1997-2001, which was approved in 1997, which summarises the development in Peru since the 1980s. I have also used several other research papers and articles about privatisation in general and privatisation in Peru. Especially I have used the works of Máximo Torero, who is for the privatisation and Teivo Teivainen, who is more critical towards both the Bank and privatisation. Different statistics and indicators of development are also primarily from the World Bank publications, especially from the World Bank Atlases. Some figures are from other development organisations publications, for example United Nations development program (UNDP).

I will examine the privatisation process in Peru in the 1990s. Peru made reforms in the beginning of the 1990s, which were very much in line with the World Bank's idea of development at that time, and privatisation was one of these reforms. The IMF and the World Bank surely influenced the government of Peru in performing these policies, but my question is not was Peru in some way forced or persuaded to implement these policies. Rather I am interested in testing the World Bank theory and to find out, did privatisation help the country develop during the 1990s? There are theories on how privatisation does benefit development and other theories arguing how it does not. Therefore I will use the available data in order to assess how beneficial privatisation is. I will consider the effects from the Bank's own neoliberal view and from more critical views. My research question is; does the World Bank's theory of privatisation work in practice? Has there been development in Peru in the 1990s? If development happened, how was it reached, what it consists of, how it is measured and who benefited from it?

In an attempt to answer these questions, I will first outline the Bank's concept of development and how it believes that privatisation will bring about this development. Then I will briefly summarise the privatisation process in Peru, after which I am able to study the consequences of privatisation to development in Peru. I will study the effects of privatisation on economic development and social development, as well as the connection between economic and social development. I will try to find both the straightforward effects, such as changes in employment and prices, as well as the more underlying changes in private and public spheres that affect people's lives.

2. WHAT IS THE WORLD BANK?

The International Bank for Reconstruction and Development (IBRD) was established at a meeting in Bretton Woods in 1946, together with the International Monetary Fund (IMF). The original mandate for the IBRD was to provide medium-term, lower than commercial interest rate loans to governments for post-war reconstruction and for the development of capital-poor area. However, the IBRD did not play a significant role in the reconstruction of the post-war Europe, because the United States decided not to channel its Marshall Aid through the Bank. The Bank began to focus on project lending for economic development.[3]

The World Bank today consists of the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA) established in 1960, which provide low-interest loans, interest-free credit and grants to developing countries. Interest-free credit and grants financing comes from the IDA. About 40 rich countries provide the money for the IDA credit and grants, but aside from IDA funds, very little of the Bank's income is provided by its member countries. IDA credits make up about one-quarter of the Bank's financial assistance. To be eligible for IDA assistance, a country must have a per capita gross national income of $865 or less. Middle-income countries, countries with a per capita income of less than $ 5,115, receive loans from the IBRD. The IBRD raises almost all its money in the world's financial markets. IBRD offers loans near-market terms, but with more time to repay than if a country would borrow from a commercial bank. In addition to IDA and IBRD, the International Finance Corporation (IFC), Multilateral Investment Guarantee Agency (MIGA) and International Centre for Settlement of Investment Disputes (ICSID) belong to the World Bank group. IFC promotes private sector investment by supporting high-risk sectors and countries; MIGA provides political risk insurance to investors in and lenders to developing countries and ICSID settles investment disputes between foreign investors and their host countries. [4]

The Articles of Agreement of the IBRD state that the purposes of the World Bank are to assist in the reconstruction and development by facilitating the investment of capital, to

[3] Toye (2003), 365

promote private foreign investment, “to promote the long-range balanced growth of international trade and the maintenance of equilibrium in balances of payments by encouraging international investment for the development of productive resources of members, thereby assisting in raising productivity, the standard of living and conditions of labour in their countries”. The purpose of IDA is to “promote economic development, increase productivity and thus raise standards of living”. The Article of Agreements prohibits political activity. It says that “The Bank and its officers shall not interfere in the political affairs of any member” and “only economic considerations shall be relevant to their decisions”. [5]

The Bank’s Articles of Agreement are quite flexible which means that they leave open a wide array of paths through which the Bank can pursue issues that it deems central to the goal of development. Even more relevant than the Articles for determining Bank practice are the range of policies, directives, and advice published by the Bank for use by its staff. The most binding of these are Operational Policies, which establish the parameters for the conduct of Bank operations. A less binding category of policy is Bank Procedures that spell out the processes and documentation needed to ensure that Bank policies are carried out in consistent manner. A third category is Good Practice, which consists of advice and guidance on how to implement policy. [6]

Miller-Adams argues that the World Bank’s culture is characterised by two key norms. First, development is seen as an apolitical process. The apolitical orientation of the Bank is embodied both in the Articles of Agreement and in the values and beliefs of its staff. Various scholars have shown that the Bank has never been as apolitical as it maintains, but the apolitical norm is an important part of the Bank’s identity and legitimacy in the eyes of the international community. The official avoidance of politics has allowed the Bank to work with a diverse group of governments and allows staff members from around the world to set aside their personal and/or national politics and identify themselves with the institution for which they work. Apolitical identity also increases the Bank’s legitimacy in the eyes of its borrowers. Pressure to avoid politics

[4] www.worldbank.org About Us – What is the World Bank and Operations
[5] Koivusalo & Ollila (1997), 24
[6] Miller-Adams (1997), 23

has come from some developing countries that oppose what they perceive as Bank interference in their internal politics. [7]

The second key norm of the Bank is that development can be achieved through technical means. The Bank has always relied on well-honed techniques that, whenever possible, involve quantitative measurement and can be applied in a wide range of countries. In the 1950s when the Bank mainly lend money for infrastructure projects, the staff consisted largely of specialists with expertise in technical areas, such as agronomy, engineering or hydrology. The influence of economists grew in the 1960s and 1970s and with the introducing of structural adjustment lending in the 1980s the financial experts joined the ranks. According to Miller-Adams, one reason for the centrality of technical analysis at the Bank is that economic development is a fairly young field and one where the standards for success are difficult to define. The World Bank relies on quantitative and economic analysis and insists that objective judgements of a country's development needs are possible. [8]

The division of labour set forth at Bretton Woods, under which the IMF had primary responsibility for short-term exchange rate management and correcting imbalances in external accounts and the Bank made long-term investments in developing projects, persisted through the 1960s. When the Bretton Woods system of fixed exchange rates collapsed in the early 1970s the tasks of these two institutions began to come closer to each other. The Fund became increasingly involved in stabilisation and the time frame of its activities lengthened. In 1980 the Bank began making structural adjustment loans which are disbursed over a shorter period than its previous loans, and are conditional on economic policy reform in borrower countries. Virtually all the Bank's loans are paid out in tranches over several years. This way the Bank can control that the borrower does meet the conditions attached to the loan. Only if the conditions are met will the Bank release future instalments of the loan. The conditions are usually the completion of a given project or the enactment of agreed-upon policy reforms. [9]

[7] Miller-Adams (1997), 24
[8] Miller-Adams (1997), 24-26
[9] Miller-Adams (1997), 15-16, 18

IBRD loans are made at market rates and are expected to earn a rate of return of at least 10 per cent or its equivalent in qualitative terms when quantification is not feasible. Cases of non-payment by member countries are taken seriously and a range of measures are brought to bear against those few governments that are late in servicing their debts to the Bank. The continued willingness of developing countries to repay their Bank debt during the 1980s debt crisis was due in large part to the fact that the World Bank continued to lend to them when almost all commercial sources of finance had evaporated. [10]

The Bank influences national policies directly through a variety of conditionalities, which mostly are linked to the adjustment loans. It uses its influence also through sector policy prescriptions and technical advice. Main pressure and conditionalities have been directed at economic reform. The Bank has indirect influence as well, through the sheer size of its lending and through its influence on other donors. [11] Kanji argues that while no conditions may be directly linked to lifting subsidies, liberalising prices and privatising, the Bank is a large investor and governments are in practice forces to implement policies, which the Bank recommends. [12]

The World Bank operates all over the world. The Bank's staff is about 10,000 who come from nearly every country in the world. In addition to the World Bank's Washington DC headquarters it has 109 country offices.[13] Formal authority in the World Bank resides with the Board of Executive Directors. However, Miller-Adams argues that the top managers of the Bank are the ones who set the agenda for the Board and whose proximity to the organisation's day-to-day operations gives them substantial *de facto* power. The Bank's staff and management share a common set of values because of their background and academic training, despite the fact that they come from many different countries. They share the emphasis on technical analysis based in the disciplines of economics and finance and the Bank's official policy of avoidance of politics. [14] The Bank recruits its staff from the most elite schools in only a few countries, mostly the United States and the United Kingdom. These similarities in

[10] Miller-Adams (1997), 25
[11] Kanji (2001), 115
[12] Kanji (2001), 115-116
[13] www.worldbank.org About Us – What is the World Bank
[14] Miller-Adams (1997), 20

background and training contribute to the Bank's conformity and belief in a single truth of the nature of development. Many staff members are economists, which gives the discipline a great deal of influence within the organisation. Economists fill many managerial positions and dominate some important units of the Bank. In general, most upper-level decision-makers are economists. The standard estimate of the number of professional economists on staff is ten economists to one non-economic social scientist. The core disciplines of the Bank remain macroeconomics, neo-classical microeconomics and financial management. While nowadays there is more pluralism within the Bank than in the past, anything that is inconsistent with the accepted economic wisdom still meets with a strong negative reaction. According to Miller-Adams, the large quantity of staff members trained at US institutions has important implications on the Bank's agenda. The political philosophy taught in US graduate schools emphasises individualism over the state and discourages the study of fields like applied welfare economics, poverty and income distribution. Miller-Adams claims that the selective hiring of the Bank staff has contributed to an identifiable belief system for Bank staff, one that accepts the idea that development is an apolitical process and relies on technical approaches to achieve it. [15]

In recent years, however, there have been implications that the Bank's one-eyed view on development could change. One case of this kind of change can be seen in the small but growing number of sociologists and anthropologists on the Bank's staff. Miller-Adams says that they know that it is difficult to transform the economics based view on development, but the non-economic social scientists have already had an impact on Bank policy in some areas. The very presence of non-economists gives more focus on the social dimensions of development. [16]

Many different countries, organisations and people can influence in the agenda of the World Bank. It borrows almost all it's funds on international capital markets and then lends the money to the developing countries. The Bank is not allowed to borrow or lend more money than its member countries have pledged, plus its reserves. This means that it depends on the capital support of its members to underpin its lending. Miller-Adams argues that the most influential actors in relation to the Bank are those industrialised

[15] Miller-Adams (1997), 29-30
[16] Miller-Adams (1997), 31

nations that provide it with capital backing. Voting power in the World Bank is heavily skewed toward those developed countries that provide the greatest capital backing for the Bank. The United States has additional influence because the Bank's president is by tradition an American selected by the United States. However, the voting power of the United States has steadily declined over the years and the voting share of the other industrialised countries has risen. [17] Each member has 250 votes plus one additional vote for each share of stock it holds. In 2006 United States has 16.39 percent of votes, Japan 7.86, Germany 4.49, United Kingdom 4.30, France 4.30, and rest have fewer than 3 percent each.[18]

Borrowing countries also have a say in Bank policies, although theirs tends to be a "negative" power, the power to say no rather than to place a new issue on the institution's agenda. Those borrowers that have access to other sources of capital in addition to the money they lend from the Bank, and large developing countries where the Bank needs to do business in order to maintain its loan volume are more powerful than the smaller and poorer developing countries. [19]
Non-state actors can also influence the Bank agenda. Especially non-governmental organisations (NGOs) in both industrialised and developing nations have had a growing impact on the Bank, mainly through public campaigns to monitor and influence its performance. There are also a number of formal channels through which NGOs provide input into Bank decision making, for example NGO-World Bank Committee and the World Bank Inspection Panel. [20]

2.1 Short history of the Bank's focus issues

In the 1950s the focus of the World Bank's development agenda was on economic growth in the form of increased production and consumption in underdeveloped countries. Idea was to give developing countries an injection of capital so that they could set their own growth processes in motion. It was believed that this would better the living conditions of the poor as the wealth would 'trickle down' from the rich. World Bank also stressed the importance of helping developing countries create the

[17] Miller-Adams (1997), 10-14
[18] web.worldbank.org: IBRD: Votes and Subscriptions and IBRD Article 5, Section 3, Voting
[19] Miller-Adams (1997), 11

prerequisites that would allow their markets to function better, because in the Bank's view, underdeveloped and poorly functioning markets were a central development problem. During the 1960s it became clear that the economic growth did not automatically benefit the poor, the wealth did not 'trickle down' as anticipated. In the beginning of the 1970s the Bank formulated new goals of development for the poor. This new formulation consisted growth, 'redistribution with growth' and special help for the poor. [21] In the 1950s and 1960s the projects of the Bank were concerned with large physical infrastructure schemes, such as dams and electricity generation. In the 1970s the composition of Bank investments started to widen, gradually including agricultural and urban development projects. [22]

Since the late 1970s there has been a rise of a development paradigm, which believes that free-market economy will solve the various problems of development. The World Bank, as well as the IMF and The World Trade Organisation (WTO) have strongly argued for this paradigm.[23] The change of development paradigm in Latin America in the 1980s was also influenced by the debt crisis. The World Bank and the IMF offered a clear solution to Latin American countries facing debt problems. Solution was more competition, openness and free markets. [24] However, paradigms do not last for ever, and for example The World Bank has soften its views on government spending and has not advocated as orthodox neoliberal policies since the late 1990s as it did in the 1980s and most of the 1990s [25].

One of the shared beliefs of the Bank's staff since the late 1970s is that neoliberal policies are the appropriate prescription for its borrowers' developing economies. Neoliberal policies call for markets, rather than governments, to serve as the key allocative mechanism within an economy. This is why the Bank favours price, trade, tax and institutional policies designed to increase the efficiency of resource allocation, especially in the area of domestic investment. These ideas are incorporated in the structural adjustment programs. These views are considered conceptually correct by development experts inside the Bank, and also by many experts outside it. Interviews

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[20] Miller-Adams (1997), 11
[21] Degnbol-Martinussen & Engberg-Pedersen (2003), 26
[22] Toye (2003), 365
[23] Wilska (2004), 120-121
[24] Wilska (2004), 124

with the Bank's personnel even suggest that it is difficult for a staff member to express or act on opinions that are seriously out of step with accepted beliefs about development. [26]

In 1979 the Bank initiated a new type of lending, called programme lending. The economic shocks of the 1970s caused a need for additional balance of payment finance in the underdeveloped countries and programme loans could be justified on the grounds that, if they succeeded, they would render themselves redundant in future. The new types of loans, structural and sectoral adjustment lending (which is now known as Development Policy lending), provided rapidly disbursing foreign exchange on condition that the borrowing government undertook economic policy changes, either economy-wide or sectorally. [27] The conditions for the Bank's structural adjustment programs (SAPs) were mostly aimed with limiting the state's involvement in economic development. The state was to withdraw from the production sphere, stop its regulatory intervention in the private sector and generally reduce its expenditure. Very clearly formulated demands were made of recipient countries to implement a specific economic policy according to the recommendations of the 'Washington consensus". The poverty alleviation which had almost disappeared from the World Bank agenda in the 1980s came back in the late 1980s when it became clear that the structural adjustment programs could have devastating impact on the poor. [28]

With the end of the Cold War at the end of the 1980s the Bank was able for the first time to acknowledge explicitly the importance of political factors in economic development, including the benefits of representative government. Despite some experimentation in the direction of trying to improve borrower countries' governance, the Bank continues to maintain that politics lies outside its mandate and that its apolitical orientation remains central to its effectiveness. [29] Miller-Adams argues that private-sector-related activities fit better than participation or governance with the

[25] Wiska (2004), 121
[26] Miller-Adams (1997), 20
[27] Toye (2003), 366
[28] Degnbol-Martinussen & Engberg-Pedersen (2003), 28
[29] Miller-Adams (1997), 24

World Bank's technical and apolitical rules and the cognitive orientation of its staff and management. [30]

In 1990 World Development Report the Bank identified it's goals to include growth with equity, reduction of poverty and the creation of better earning opportunities for the poor, improved access to education, health services and other social services and direct assistance to those living under the worst conditions.[31] World Development Report from 1997 signals a shift back to recognising that the state has an important role in poverty reduction, but the liberalisation agenda still dominates. However, the Bank's focus on decentralisation and strengthening the capacity of local governments has been criticised for not acknowledging that both strong central and local governments are required for effective poverty reduction. [32]

2.2 The World Bank view on development in the 1990s – the roles of public and private sector

My intention is to study the development in Peru between 1990 and 2001, which is why I will focus on the World Bank view on development in that decade. I have searched both the Bank's publications and some more critical texts for the World Bank idea of development and how to achieve it.

As it is outlined in many World Bank publications, the essential task of development is to provide opportunities so that people (and especially the poor), can reach their full potential.[33]
"Development is about people and their well-being – about people developing their capabilities to provide for their families, to act as stewards of the environment, to form civil societies that are just and orderly. Human capital development – the result of education and improvements in health and nutrition – is both an end and a means to achieving social progress. Human capital is crucial to raising the living standards of the poor. Because the poor's most significant asset is their labor, the most effective way to

[30] Miller-Adams(1997), 32
[31] Kegnbol-Martinussen & Engberg-Dedersen (2003), 28
[32] Kanji (2001), 125-126
[33] for example The World Bank Atlas, 25th Anniversary Edition 1992, 7 and The World Bank Atlas 1995

improve their welfare is to increase their employment opportunities and labor productivity through investments in human capital. The poor are often unable to finance such investments."[34]

Development is essentially about people and their well-being, which I believe is very commonly approved concept of development. Differences of opinion rise when one needs to decide on how to reach development and how it is possible to measure whether development has occurred or not. The World Bank has its own, widely accepted idea of development. As the improvement of the lives of the poor, and others, demands investments, and the poor do not have the money to make these investments, someone else has to make them. Whether it is the government or the private organisations or companies, economic growth is needed to increase these investments.

The path to economic development, which the Bank advises for the developing countries, includes switching to an efficient, labour-intensive pattern of development and investing in the human capital of the poor. This contributes to the faster long-term economic growth. [35] Investment in the human capital of the poor includes for example education and health care. These are in the Bank's speech often argued to be important as a way to get poor people participating in the economic growth and that way bettering their lives.

The World Bank has outlined few characteristics, which in its view have benefited development in the past. These include commitment to better policies for macroeconomic management, open-door policies toward foreign trade and foreign investment that contribute to closer integration with the global economy, strong growth of the service sector and expanding trade in services and a decreasing share of central government spending in GDP. [36] The Bank sees that the domestic route to economic growth is capital accumulation through savings and investments, and the external route is export expansion and diversification. From these goals are derived the policies that the Bank advocates – fiscal and monetary probity, a sound currency, external economic

[34] The World Bank Atlas 1998, 18
[35] World Development Report 1990, 3
[36] World Bank Atlas 1998,

equilibrium, expert dynamism, economic stability, and a favourable investment climate. [37]

The World Bank has demanded the reduction of the role of the state in order to achieve economic growth. Reason for this is based on the neoliberalist view that state must not interfere in the market sector. The ideology is that the private sector commercial operations are generally more efficient than those of the public sector and that private markets result in a more efficient allocation of resources than public provision. Thus the World Bank demands that the production and the provision of the services are shifted from the public sector to the private sector, that the level of governmental expenditures are restricted and that regulations which affect transactions in private markets are removed. [38] According to Todaro, privatisation relies on the neoliberal hypothesis that private ownership is more efficient and develops more rapid economic growth. The belief is that privatisation improves efficiency, increases output and lowers costs. Proponents argue that it curbs the growth of government expenditure, raises cash to reduce public internal and external debt and promotes individual initiative while rewarding entrepreneurship. Finally, the supporters of privatisation see it as a way to broaden the base of ownership and participation in the economy, thereby encouraging individuals to feel that they have a direct stake in the system. [39]

The reason why the World Bank started to demand these economic policies from the developing countries can be found in recent history. In the beginning of the 1980s many Latin American countries had severe economic difficulties. Markets were not functioning well, GNP declined for three consecutive years and budget deficits were high, in some countries 5-10 per cent of GDP. The Washington Consensus of US economic officials, the International Monetary Fund and the World Bank was designed to answer to these problems. Consensus saw inflation as the biggest obstacle to macroeconomic stability. Second component to stability was reducing the size of the government, the budget deficit and the account deficit. Economic development was to be achieved through trade liberalisation, deregulation and privatisation. According to

[37] Koivusalo & Ollila (1997), 28
[38] Koivusalo & Ollila (1997), 32
[39] Todaro (1997), 631

Stiglitz, these are still important policies but others like competition, education and improvement of technology need to be added in the New Consensus.[40]

In the 1998 Annual World Bank Conference on Development Economics publication Wolfensohn writes that

> "Sound monetary and fiscal policy are important for an open market, as are many of the tools and visions of economics described in the so-called Washington Consensus". [41]

But he as well says that among the development economists, there is a general agreement that the Washington Consensus is dated and it needs to be modified. He as well speaks of a New Consensus, which acknowledges that it is crucial to have economic growth and to adhere to tried and true monetary and fiscal policies. But in time larger concerns are for equity and social justice. Wolfensohn summarises that this New Consensus includes education, which is "the key to unlocking equal opportunity", next is health care, and then infrastructure, justice system, elimination of the economic distortions created by crime and drugs and ensuring the civil safety. Other important factors are well functioning financial systems, urban and rural strategies, and power, sanitation and communications services. "But of course, good macroeconomic policy and open trade must be part of these efforts".[42]

It is clear in both old and new Consensus that the Bank advocates the participation of private sector in many areas of economic and social development. State and private sector both have roles in development, but often the private sector seems to be the better choice. Public sector should do something if the private sector is not willing to do it. The Bank states for example that

"the diversity of experience makes it difficult to draw conclusions about what makes states and markets effective – and what size state is right for any set of social and economic circumstances. In 1996 ratios of central government spending to gross domestic product ranged from less than 10 percent to about 50 percent. Different types of governments are looking for ways to freeze and eventually cut this spending without

[40] Stiglitz (1998), 4-5,9
[41] Wolfensohn (1998), 59
[42] Wolfensohn (1998), 59-60

losing votes. Many developing country governments are shifting their priorities from preserving jobs in a stagnant public sector to creating jobs in a vibrant private sector. This shift implies a fundamental change in the role of government – from owner and operator to policy-maker and regulator, working closely with the private sector to develop a competitive, outward-looking economy. The market is often the most acceptable and efficient solution – with private health and unemployment insurance, private contributions to education costs and care for the elderly, and even private prison services among reforms initiated in the 1990s." [43]

> "The challenge for developing countries is to provide as good an institutional framework for development as their capabilities will allow. Governments should not intervene where markets can operate more efficiently, but governments should ensure that the rules of the market and the laws of the state are applied fairly and equitably to all."[44]

Joseph Stiglitz, in 1998 when he was a chief economist of the World Bank, stresses the importance of broadening the objectives of development from good economic performance to sustainable development, egalitarian development and democratic development. [45]

"The post-Washington consensus recognizes both that a broader set of instruments is necessary and that our goals are also much broader. We seek increases in living standards – including improved health and education – not just increases in measured GDP. We seek sustainable development, which includes preserving natural resources and maintaining a healthy environment. We seek equitable development, which ensures that all groups in society, not just those at the top, enjoy the fruits of development. And we seek democratic development, in which citizens participate in a variety of ways in making the decisions that affect their lives."[46]

The World Bank conducted a study East Asian Miracle in 1993 and found that East Asian development strategies included aspects which were not emphasised by the Washington Consensus, such as egalitarian policies and even some which were contrary

[43] World Bank Atlas 1998, 44
[44] World Bank Atlas 1998, 44
[45] Stiglitz (1998), 1
[46] Stiglitz (1998). 31

to the spirit of the Washington Consensus. Here Stiglitz refers to the East Asian industrial policy, which was designed to close the technological gap between these countries and the more developed countries. These observations stimulated the Bank to rethink the role of the state in economic development in the mid-1990s. [47]

The Washington Consensus policies were based on a rejection of the state's active role in development. The Consensus promoted a minimalist, non-interventionist state and the unspoken premise was that governments are worse than markets. Stiglitz agrees that states are often involved in too many things and feels that the states should focus on the things that states only can do. These would be economic policies, basic education, health, roads, law and order and environmental protection. In his view, the question is not whether the state should be involved but rather how it gets involved. The issue is not the size of the state but the activities and methods of the state.

In the late 1990s it was also realised that the government and the private sector are more intimately entwined. According to Stiglitz, the government should be a complement to markets, to undertake actions, which help the markets, work better and correct market failures. Government can also be a catalyst for private sector, but once the catalytic role has been performed the state needs to get out of the way. World Development Report 1997 sees an effective state as vital for development. In addition to economic policies and human capital, the quality of a country's institutions, like an independent judiciary and separation of powers, determine economic development. [48]

Regulation serves four purposes in financial markets. Maintaining safety and soundness, promoting competition, protecting consumers, and ensuring that underserved groups have access to capital. Also social objectives can, if done well according to Stiglitz, reinforce economic objectives. The Washington Consensus was created in time when financial systems were highly regulated and many of the regulations were designed to limit competition rather than promote above-mentioned objectives of regulation. Stiglitz argues that the dogma of liberalisation has too often become an end in itself and not as a mean to achieve a better financial system. [49]

[47] Stiglitz (1998), 2
[48] Stiglitz (1998), 24-29
[49] Stiglitz (1998), 15-16

The World Bank president James D. Wolfensohn said in 1996 that his goal was to make the Bank “quicker, more effective, more agile, and more responsive to its clients”. He emphasises the importance of research and thinking in the Bank’s goal to improve results on behalf of developing countries. He says that the Bank’s role is to

> “identify and seek out the best ideas, develop their practical applications and get them to end users (in developing countries) in time to apply them to the real problems people face“. [50]

Wolfensohn’s choice of words implies that the need for development comes from the people in the developing countries, but the Bank has the know-how to achieve development. It has the experience, resources and knowledge needed for development.

The Bank has often been criticised for its top-down stance on development problems. It develops a lending program in line with its own diagnosis of a borrower’s problems and gives the technical skills and financing it believes are needed to address those problems. In Miller-Adams’s view, the Bank has begun to acknowledge that it needs to consult outside groups in it’s lending policies, but the top-down, expert-oriented approach to lending remains very much intact. [51]

The World Bank has a strong influence on development field and the neoliberal orthodoxy embraced by the Bank in the 1980s and 1990s has repercussions beyond the institution. The relationship between the Bank and the wider community of development experts, for example those in government, academia and think tanks, is mutually constituting. The World Bank is not only an organisation that receives and carries out the tenets of development ideology; it is also a contributor to that ideology. The input of development experts from outside the Bank into its reports demonstrates the reciprocity of influence between the organisation and the broader development community of which it is a part. [52]

[50] Wolfensohn (1996), 9
[51] Miller-Adams (1997), 17
[52] Miller-Adams (1997), 20

The World Bank is commonly viewed as the principal teacher of economic development in the world today. With the U.S bilateral aid agency (AID), they largely determine the ideology and operational model of a host of UN and regional agencies. By subcontracting they mould or control dozens of private groups and consulting firms. Their shared norms about economic development influence most bilateral and practically all multilateral institutions. [53]

2.3 How the World Bank measures Development

For the purposes of the World Bank, development needs to be something that can be measured and expressed with numbers. Economic growth has been the first, most important and easiest indicator. For the Bank, economic growth can be seen both as a goal for development and as a mean to reach social and human development. Economic growth is the most important indicator for development that the Bank uses and growth is measured with gross domestic product (GDP). Economic growth is essential, as it makes a country and its people more prosperous and developed. However, as stated earlier, the Bank has widened its perspective on development since the late 1960s to include other indicators than economic ones. At present, the Bank measures development with various indicators, for example environmental, infrastructure and social indicators, economic statistics and figures of gender equality.

The 25th Anniversary edition of the World Bank Atlas in 1992 introduced new indicators for measuring development. It states in its introduction, that the Atlas "presents key social and economic information organized under three headings, People, Economy and Environment, to emphasize the importance of these themes in the development process. In this edition, new data and maps have been introduced covering such topics as child mortality rates, female labor force, and various aspects of the environment."[54] The World Bank Atlas 1996 explicitly states that economic growth has straightforward impact on social development.

"In the last ten years, nearly 100 countries have experienced overall growth in per capita income, and evidence suggests that the level of poverty declines as an economy

[53] Wood (1986), 106

expands." "Many of these Latin American (Chile and Uruguay were mentioned) and Asian countries also have high levels of literacy, reflecting the link between basic education and growth". "Infant mortality rates across all developing countries have almost halved, from 96 in every thousand births in 1970, down to 55 in 1993." "Average life expectancy for high-income countries rose from 71 in 1970 to 77 in 1993, but the low-income population still has an average life expectancy of only 62 years." "In most parts of the world women make up more than 30 percent of the labor force, in 20 countries women still form less than 20 percent of the formal work force." "It is these issues, and others, that the Atlas highlights each year in an effort to strengthen global understanding of the measures of development." Despite all of this success "much development work remains".[55]

The World Bank Atlas 1998 states that over the past 25 years "per capita income growth in developing countries averaged more than 1,4% a year". "Although the number of people living in poverty continues to grow…the proportion of the poor is holding steady at less than a third of the developing world's population". [56]

There are many problems when estimating development from statistics. One problem of measuring development is that average numbers of development indicators, be they economic ones or social statistics, do not show how the development is spread across the country. If under five mortality rate has decreased in ten years in a given country, this does not tell us whose children have survived, children of the rich or the poor or perhaps both. If the health care and nutrition of children of rich families has bettered so that all of them live to see the age of five, the poor children can have under five mortality rates in the same level as ten years ago, or even worse. Another problem is that in developing countries the statistics are not necessarily very accurate. Even basic data such as population are often only estimates.

[54] The World Bank Atlas, 25th Anniversary Edition 1992, 3
[55] The World Bank Atlas 1996, 3
[56] The World Bank Atlas 1998, 18

2.4 The Bank's view on poverty in the 1990s

The World Bank saw economic growth as the primary means of reducing poverty and improving the quality of life in the 1950s and 1960s. In the 1970s attention shifted to the direct provision of health, nutrition and education for the poor. In the 1980s the Bank started to focus on the problems the developing countries had in adjustment after the global recession. The constraints on public spending tightened and many began to question the effectiveness of direct provisions toward the poor. This was the background against which the Bank says it started to re-examine its policies aimed to reduce poverty in late 1980s. [57]

In the World Development Report in 1990, in which the focus is on poverty, the Bank argues that because of the macroeconomic crises of the 1980s many developing countries needed to go through a "period of painful macroeconomic adjustment", but in the longer term the economic restructuring associated with adjustment is perfectly consistent with the poverty reduction. In the short term, however, "many of the poor are at risk." The Report says that there are various policies to cushion the impact of adjustment on the poor, which can be used. However, the Bank's experience since the 1970s shows that reaching the poor with targeted programs can be difficult. In order to be affordable and hence sustainable, these programs should in Bank's view be cost-effective. Well designed and accurately targeted public spending can play an important role in the fight against poverty. Fighting poverty should not be left only for special programs, it must be a task for economic policy in large. [58]

For the Bank, reducing poverty is the fundamental objective of development. The Bank sees it as a task for governments to develop strategies and policies to fight poverty. Knowledge about the poor is essential if governments are to succeed in this task. The Bank divides the poor into two main groups: the urban poor and the rural poor. The Report defines poverty as the inability to attain a minimal standard of living. In measuring this standard of living, the Bank uses the consumption-based poverty measure and supplements it with social indicators, such as nutrition, life expectancy, under 5 mortality and school enrolment rates. A consumption-based poverty line can be

[57] World Development Report 1990, 2

thought of as comprising two elements: the expenditure necessary to buy a minimum standard of nutrition and other basic necessities and a further amount that varies from country to country, which reflects the cost of participating in the everyday life of society. [59]

The Bank acknowledges that the perception of poverty has evolved historically and varies from culture to culture. In general, as countries become wealthier, their perception of the acceptable minimum level of consumption – the poverty line – changes. The Bank uses a universal poverty line, which helps to make cross-country comparisons and aggregation. The poverty lines used are $ 275 and $ 370 per person a year. [60] From these the $ 370 a year is the most often used one, $ 1 a day. Poverty line is a median of the poverty lines of ten poorest countries[61].

Since the publication of the 1990 World Development Report, poverty reduction has officially remained the first priority for the Bank. Later it has formulated its commitment to poverty reduction by introducing the ‘three-pronged strategy’, which is based on three pillars: broad-based growth, human capital development and safety-nets for the poor. According to Nazneen Kanji, this explicit formulation of poverty reduction does not differ greatly from the Bank’s older view, which sees the poverty reduction as an expected consequence of economic growth. Broad-based growth means labour-demanding growth pattern that can provide increased employment and income. The main approach to achieve this is through a minimalist state, undistorted markets and the public provision of infrastructure, which stimulates and facilitates investment in the private sector. The second prong is the development of human resources through the provision of primary health-care and education and other basic services. At present, the Bank sees investing in services rather in terms of human capital than basic needs or basic rights. Increasing access to services is seen instrumental in that it promotes economic development. The third prong is the provision of safety-nets. Safety-nets are basically income maintenance programmes that protect people against adverse

[58] World Development Report 1990, 3-4
[59] World Development Report 1990, 24-26
[60] World Development Report 1990, 27
[61] Tammilehto (2003), 28

outcomes such as chronic incapacity to work and earn, and a decline in this capacity caused by for example bad harvests or economic recession.[62]

Kanji criticises the Bank's understanding of poverty reduction, because it pays little attention to the distribution of assets in society. Assets here mean both material resources such as land and capital and non-material resources such as political power and social organisation. [63] However, the World Bank has acknowledged this explicitly in its publications. For example the 1990 Development Report states that the link between average levels of income and social indicators of development can vary in different areas. This in Bank's view underlines the need to look beyond average incomes to the distribution of income and the provision of social services. [64] However, the Bank does not recommend policies, which would change the distribution of incomes in any significant way.

The Bank acknowledges that the burden of poverty is spread unevenly and weight of poverty falls most heavily on certain groups. Women in general are disadvantaged, and so are as children.[65] In many countries poverty is correlated with race and ethnic background. For example in Peru, the indigenous people are disproportionately represented among the poor. In general, poor have less access to publicly provided goods and infrastructure than other groups. The poor usually have to use substantial amount of their incomes in food. Data from Peru in 1985 shows that about 70 percent of the expenditure of poor households was spend for food. The corresponding figure for all households was about 50 percent. Poverty is often the fundamental cause of malnutrition. [66] The problems of malnutrition, lack of education, low life expectancy and substandard housing are, as a rule, more sever in rural areas. This is true also in Latin America, despite high urbanisation rates. The Andean areas of Bolivia, Ecuador, Guatemala and Peru are areas of concentrated poverty. In Latin America, the worst poverty occurs predominantly in arid zones or in steep hill-slope areas that are ecologically vulnerable and isolated in every sense. [67]

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[62] Kanji (2001), 111-113
[63] Kanji (2001), 114
[64] World Development Report 1990, 29
[65] The World Bank Atlas, 25th Anniversity Edition 1992, 7
[66] World Development Report 1990, 36-37

The World Bank took a new step in poverty reduction in the annual meeting between the IMF and the Bank in 1999, when the two institutions decided that poor countries should make a national strategy to reduce poverty. Idea was that in the future development aid and loans, and debt relief were to support these Poverty Reduction Strategy Papers (PRSP). In the beginning of 2003, twenty countries had prepared PRSP and forty were in a process of doing their own. Critics have said that the PRSP's of different countries are surprisingly similar with each other. What more, they are similar to the earlier structural adjustment programs as well, with great emphasis on free-trade ideology. [68]

[67] World Development Report 1990, 29-30
[68] Wilska (2004), 132-134

3. PRIVATISATION AND DEVELOPMENT

There are various reasons why the developing countries have created and still maintain the state-ownership of various enterprises and services. One of the reasons is the persistence of monopoly power in many developing countries. Direct government control may be required to ensure that prices are not set above the marginal costs of producing the output. Certain goods that have a high social benefit are usually provided at a price below their costs or even free, which of course means that the private sector has no incentive to produce such goods. Capital formation is also an important rationale for the creation of state-owned enterprises, especially in underdeveloped countries where the private savings are very low. State's investment in infrastructure is important to lay the groundwork for further investment. The lack of private incentive to engage in promising economic activities because of factors such as uncertainty about the size of local markets, unreliable sources of supply and the absence of technology and skilled labour is a major motivation for the creation of public enterprises. Other reasons for the creation of state-owned enterprises is the desire of some developing countries' governments to gain national control over strategic sectors of the economy such as defence, and over foreign-owned enterprises whose interests may not coincide with those of the country, or over key sectors for planning purposes. Ideological motivations may also be a factor in the creation of state-owned enterprises. [69]

Despite these many good reasons for their existence, the state-owned enterprises have come under increasing attack in recent decades. State-owned enterprises are accused of wasting resources and they make significant demands on government finance, as well as on domestic and foreign credit. In many cases, the level of these demands is related to low profitability and inefficiency. It is difficult to generalise across countries, but the World Bank's data about state-owned enterprises in 24 developing countries revealed only a small operating surplus and after taking account the interest payments, subsidised input prices and taxes and accumulated arrears many of these enterprises showed a large deficit. Also labour and capital productivity are often lower in state-owned enterprises than in private firms. [70]

[69] Todaro (1997), 630

Several factors contribute to the overall poor performance of the state-owned enterprises in terms of profitability and efficiency. Perhaps the most important is that state-owned enterprises differ from private firms in that they are expected to pursue both commercial and social goals. Providing goods at prices below costs in an effort to subsidise the public or hiring extra workers to meet national employment objectives inevitably reduces profitability. Another factor adversely affecting the profitability and efficiency of state-owned enterprises is the over-centralisation of their decision making which allows little flexibility for managers in the everyday operation of the firm. An additional problem is the bureaucratisation of management. Many decision-makers are not accountable for their performance and little incentive is provided for improved decision making. Finally, access to capital at subsidised interest rates has often encouraged unnecessary capital intensiveness. [71]

David Macarov says that there are various ways in which privatisation can be defined. I will use the same one which he says to be the most common meaning: "Privatization is the shifting of governmental functions and services to non-governmental entities, either to voluntary not-for-profit organizations, or to for-profit businesses."[72] Privatisation includes also the transfer of property rights from the state to a private entity. Property rights include control rights, return rights and alienation rights. Control rights means the rights to utilise the asset, return rights means the right for any benefits which might come from the asset, but also the responsibility for any negative outcomes, and finally alienation rights mean the right to buy and sell the asset or portions of the asset or to transfer all or part of the other rights to someone. Privatisation principally involves the legal transfer of property rights from the state to individuals, but in many cases not all three rights are transferred.[73]

3.1 Why does the Bank encourage privatisation?

When the oil-price shock in 1973 triggered economic problems of high inflation and economic stagnation that were not resolved by conventional Keynesian policies, the neoliberal paradigm became more and more dominant. The role of the state in the

[70] Todaro (1997), 530
[71] Todaro (1997), 530-31
[72] Macarov, (2003), 68

economics and the state-owned enterprises became under attack by many economists. Initially, emphasis was placed on the distortion in prices and quantities derived from state action, but the critique later centred on the inefficiencies in the public allocation of resources compared with the private allocation, which was seen as more efficient. Privatisation was advocated as the answer to improve both microeconomic and macroeconomic performance. [74]

The main goals of all privatisation's advocated by the World Bank are to promote the private sector as an engine of economic growth and to increase efficiency and productivity in the economy. In general, it was assumed that privatisation policies would improve efficiency of resource use, foster competition, enhance the role of the private sector, obtain higher rates of domestic savings and investment and attract and provide opportunities for foreign investors. The SAPRI report categorises the stated objectives of the privatisation process in three main groups: economic objectives, fiscal objectives and social and political objectives. Economic objectives include improving the overall efficiency of the economy, improving the efficiency, productivity and profitability of firms, and improving the quality of products and services and attracting foreign investment. Fiscal objectives are reduction of government subsidies to public enterprises, raising money from the sale of state-owned enterprises and increasing tax revenue from private enterprises. Social and political objectives consists of improving the welfare of society, promoting the ownership of private enterprises by nationals, creating a property-owning middle class, increasing total employment in the economy and reducing corruption and the abuse of public office. [75]

As the World Bank sees the private sector as the best way to increase economic growth, it aims at promoting business of the private sector. The key technique how the Bank does this, is the "strategic nonlending". This means that the Bank will refuse to finance a project for which private investors or lenders can be found, thus forcing the aid-seeking government to accept the terms of the private investors or lenders or go without external financing. The Bank can also withhold aid from projects which private investors cannot be found in order to influence government policy to foster a more

[73] Honkkila (1997), 11-12
[74] Structural Adjustment, The SAPRI Report (2004), 111-112
[75] Structural Adjustment, The SAPRI Report (2004), 112

satisfactory investment climate. In Wood’s view, the function of strategic nonlending is to maximise the role of the private sector and to open it to foreign penetration. [76]

The most important form of strategic nonlending is sectoral withholding, in which donors “reserve” certain sectors for private capital and withhold aid from them. Since the end of the WWII, the sectors that have been identified as potentially the most attractive for private investors and therefore denied aid most consistently have been mining and manufacturing. Aid has been used primarily to create the physical and social conditions for private investment in these sectors, to create an infrastructure. Wood argues that the primary goal of sectoral withholding is to prevent state ownership of the means of production. When this goal is achieved, it forces the state to be both politically and financially dependent on processes of private capital accumulation. [77]

The policy of avoiding competition with the private sector is part of the constitutions of each part of the World Bank Group. The Bank and also other development banks are prepared to approach private banks and investors on their own to ensure that the loans they are considering cannot be privately financed. The fact that in most cases private capital will be foreign capital is considered irrelevant and it does not justify the use of Bank loans as an alternative. [78]

The Bank also insists that consumers of public utilities should bear the full cost of the services they receive. In other words, these services should not be subsidised by society as a whole. This principle has traditionally applied primarily to electricity and running water, but there is a clear tendency to extend it. For example to irrigation, agricultural credit and urban sites and services schemes. Even in the social sectors like health and education, the Bank feels that “a modest reduction in the subsidy for some services may be appropriate”. [79]

[76] Wood (1986), 115
[77] Wood (1986), 117
[78] Wood (1986), 115
[79] Wood (1986), 115

3.2 Privatisation process in Peru

The ownership of land and other property has changed between the state and private owners in the history of Peru. Indians have traditionally owned their land communally, but the economic recovery in the late 19th century strengthened the political hand of the planter aristocracy and the commercial bourgeoisie, and the sugar plantations on the coast expanded at the expense of small landholders and Indian communities. In the Andes the economic revival spurred a renewed drive by landowners to acquire Indian communal lands. By the 1920s almost all land in Peru was individually owned and worked. [80] Economic growth attracted also foreign investors and at the end of the 1920s the mines and oil-wells which were the principal sources of Peru's wealth, were nearly all foreign owned, and excepting for wages and taxes, no part of the value of their production stayed in the country.[81]

The state ownership expanded in the late 1960s, as "the Revolutionary Government of the Armed Forces" (1968-1975), under the leadership of General and President Juan Velasco Alvarado decreed the nationalisation of oil, an agrarian reform law and a law providing for workers' participation in the ownership and management of industrial concerns. The dominant ideology in the armed forces at that time stressed the need for planning, industrialisation, land reform and an expanded directing role for the state. The major objectives of a land reform were to expand agricultural production and to generate capital for investment in the industrial sector. Landowners were compensated for expropriated lands with bonds that could be used as investment capital in industry or mining and the recipients of land were required to pay the purchase price over twenty years. The land reform ended the various forms of serfdom that still existed in the Sierra in 1968. The reform increased food production a little, and it proved to be a major economic and political benefit to a significant sector of the peasantry, as the wages rose and the quality of life improved. However, the reform failed to raise the general material and political level of the majority of Peruvian peasants. As a considerable

[80] Keen (1992), 388, 391
[81] Keen (1992), 384-93

amount of land escaped expropriation, the reform made only a slight impact on the problem of landlessness and rural unemployment and underemployment. [82]

When the military revolution began in 1968, foreign firms controlled the most important sectors of the Peruvian economy. By 1975, state-owned enterprises had taken over most of these firms. The state came to control decisive sectors of the economy. The military government tried to give incentives for industrial investments to the local bourgeoisie, but they were not satisfied with the radical nationalist rhetoric of the junta and failed to respond to the incentives. As a result, the government had to be the main investor and by 1972 accounted for more than half of the total investment in the economy. These investments, land reform and nationalisation of foreign enterprises were getting too expensive for the government. Peru could not apply for loans to the United States or the multinational agencies, which the U.S controlled because of disputes over expropriation. Therefore Peru loaned money from foreign private banks: Peru was the largest borrower among the underdeveloped countries in 1973 with its $734 million loans. By 1975, the prices for oil and imported equipment and technology were rising while prices for Peru's raw material exports were falling, which created unmanageable balance of trade and debt service problems. Keen argues that "the model of development based on export expansion and foreign borrowing had again revealed its inherent contradictions". [83] Despite Velasco's anti-imperialist tendencies, Peru was in his time a relatively attractive destination in private loan markets. However, the extensive use of external borrowing by the Velasco government made Peru vulnerable to the effects of the debt crisis earlier than most other countries of Latin America. [84]

Teivainen argues that the economic policies in Peru after 1975 can be seen as a gradual dismantling of Velasco's nationalist reforms. The importance of state activities as a percentage of the GDP has diminished since 1975, even during the ideologically state-interventionist years of Alan García's government in 1985-1990. In 1975 state accounted for 21,4 % of the GDP and in 1989 its share had dropped to 11%. [85]

[82] Keen (1992), 397-8
[83] Keen (1992), 399-400
[84] Teivainen (2000), 92
[85] Teivainen (2000), 6

The economic crisis of 1975 resulted in a peaceful coup. In order to appease foreign and domestic capitalists, the new Francisco Morales Bermúdez government put an end to reforms of the previous government and introduced a package of austerity measures that called for reductions of the state economic sector, cuts in budgets and subsidies, increases in consumer prices, restraints on wage increases, and a 44 percent devaluation of the currency. These policies provoked strikes and rioting, but the government crushed protests with military operation. [86]

New constitution was drafted for Peru in 1979. The new constitution was ambiguous as regards the role of the state in economic sphere. It stated that the state could have extensive direct intervention in the economy through public enterprises and other means. Emphasis was on state planning. State was obliged to formulate its economic and social policies through development plans. Constitution also advantaged national private investments over foreign private investments.[87]

Second Fernando Belaunde government (1980-1985) was mostly in line with the IMF's and the World Bank's neoliberal economic policies and the Peruvian exporters, but tried to maintain the idea of national sovereignty in economic policies and not of submission to the international organisations demands. The leading sectors of military were opposed to radically neoliberal reforms, but the business elite supported them. However, in 1983 the support for orthodox economic policies declined in all sectors of society. For example in 1983, Annual Conference of Business Executives (*Conferencia Anual de Ejecutívos*, CADE) called for a "realist national plan" which reflected the growing discontent of entrepreneurs toward the 'neutral' economic knowledge of the IMF and the Bank. Economy Minister Carlos Rodríguez Pastor in the same conference asked the critics to stay calm in order to assure the continuous help from the IMF and the World Bank. Although Rodríguez Pastor's policies were far less radically neoliberal than Fujimori's in the 1990s, he had to resign in 1984. [88]

Most of the Peruvians blamed the economic crisis in the beginning of the 1980s on Belaúnde government's policies and especially on its debt payment and austerity

[86] Keen (1992), 400-1
[87] Teivainen (2000), 35-96
[88] Teivainen (2000), 98-101

programs. This discontent resulted in Alán García Pérez's victory in presidential election in 1985. García campaigned on a populist, reformist program. He promised to defend the agrarian and industrial reforms of the military junta's era and to reject the free market policies of the Belaúnde regime. García also proclaimed that Peru would limit interest payments on foreign debt, which at this point was about $14 billion, to ten percent of export earning - about $400 million a year. Limitation of debt payments was designed to make capital available for the development of Peru. His economic program also included measures to halt capital exports, freeze the price of necessities, and raise the minimum wage by 50 percent. His long-term goal was to promote the development of "an autonomous Peruvian capitalism based on expanded import-substitution industrialisation and reduced dependence on imported raw materials". [89]

In 1986 Peru's ratio of debt to GNP was as high as 74,1%. Peru's debt problem attracted great attention outside Latin America in the late 1980s because of the debt repayment policies adopted by President Alan García.[90] The IMF demanded a payment plan from Peru or it would declare Peru ineligible, which would mean a marginalization of the country from international capital markets. Peru did present a plan in 1986, which was soon accepted by the IMF. However, the Alan Garcìa government failed to honour the agreed-on timetable of payments and the IMF declared Peru ineligible for further credit. Peru would have been able to follow the agreed timetable of payments, but according to Teivainen, it made a decision not to. The ineligibility declaration of the IMF made it very difficult for Peru to find external funding and the country was financially isolated. The World Bank stopped its funding to Peru at the beginning of 1987. [91]

The IMF and World Bank are institutions that the foreign officials, bankers and investors listen to when deciding whether to invest or assist a country or not. If these institutions refuse to give credit to a country, it is hard for that country to get credit from anywhere else as well. [92] The World Bank effects on the borrowers' image towards other investors and lenders. Bank approval of a country's economic policy, signalled for

[89] Keen (1992), 403
[90] Third World Economic Handbook (1989), 118
[91] Teivainen (2002), 74-77
[92] Wilska (2004), 124

example by a large adjustment loan, is an important factor in establishing that country's creditworthiness. [93]

By mid-1987 it was clear, that Peru's domestic business elite did not invest enough to compensate the lack of external financing. President Garcìa then had a choice between giving in to the business demands, or to take a more state-interventionist stand. García chose the latter, and declared that the state would take possession of the private banking and insurance companies. He said that this had to be done in order to defend Peru's "economy in front of the debt crisis". According to him, too much economic decision-making power had been transferred to the financial sector and that Peru had been governed by "groups articulated with transnational power". Until then he had waged his war against imperialists outside Peru, but now he said that the frontline of this struggle existed inside Peru. García's attempt towards nationalisation did not please the business elite of Peru and they lost their confidence on the president. Business elite began to demand reinsertion into the global economy and wanted Peru to have better relationship with the IMF. The basis for Garcia's 'debt rebellion' ceased to exist when even most of his party members and the Peruvian moderate Left asked him to make peace with the IMF.[94]

According to Teivainen, the economic-policy packages in 1988 were almost a classical adjustment programme with its orthodox recipes. When presenting the adjustment packages, the Economy Minister Abel Salinas said that it would mean scarcity and discipline. "After this orthodox turn, salaries fell dramatically in real terms, inflation accelerated and the popularity of Alan García stumbled".[95] In late-1988 García finally gave in and announced that it was necessary to start negotiations with the IMF. In 1989 the government of Peru had to make many concessions to avoid the threat of being expelled from the IMF. In the agreement with the IMF in December 1989 Peru accepted the entrance of an IMF mission to study the outlines of an economic policy that would serve as a basis for the elaboration of a middle-term economic programme. This study was to be carried out together with Peruvian functionaries. Peru also resumed regular payments to the IMF. [96] Thus, in many ways the transition to neoliberalism advocated

[93] Miller-Adams (1997), 19
[94] Teivainen (2002), 94-97, 105
[95] Teivainen (2002), 103-104
[96] Teivainen (2002), 107

by the IMF and the World Bank started already in the latter half of the García government. However, “it was only after the inauguration of the presidency of Alberto Fujimori in 1990 that neo-liberalism would ascend to a dominant position within the government”.[97]

In the 1980s Peru faced large and prolonged periods of inflation and recession. The economic model that the government implemented in response to the crises assigned the state a central role in economic policy-making. According to Torero, these policies were not up to the challenge at hand. Public expenditure and public internal credit rose impressively, price controls and subsidies were established, tariffs on public services were fixed and exchange rate controls were set. According to Torero, the result was a persistent fiscal imbalance and considerable drop in tax revenues. In addition, Peru faced a high underemployment rate and a decline in financial intermediation. At the end of 1980s, inflation had reached an annualised rate of 36,000 percent and per capita income had dropped to its lowest level since the 1960s. The economic crisis affected especially the poor in Peru and their situation worsened as public services, such as education and health, deteriorated and unemployment and underemployment were high.[98]

During the presidential campaign Alberto Fujimori’s discourse was quite vague and populistic, he seemed to favour a non-orthodox, mildly left-leaning economic policy. He was against the neo-liberal shock treatment, which his opponent Mario Vargas Llosa advocated. However, when Fujimori was elected as president his views changed and on 8th of August 1990 a package of harsh adjustment measures was announced. This *fujishock* implied extraordinary increases in prices of many basic foodstuffs and fuels. Fujimori has argued that his policy switch was influenced by new information about the size of the budget deficit that he obtained only after he was elected. Teivainen argues that pressures coming from the IMF and the World Bank have played an important role in convincing Fujimori to change his mind. “The message he received from the IMF, the World Bank and the Inter-American Development Bank (IDB) was clear: make an adjustment along our policy lines if you want to get help from multilateral financial institutions”. One of Fujimori’s most urgent tasks was to improve the relationship

[97] Teivainen (2002), 108
[98] Torero (2003)

between Peru and the multilateral financial institutions. After long negotiations and adjustments, Peru was able to reinsert itself to the world-system and was eligible for the loans again.[99]

President Fujimori had at first specifically announced that there would be no large-scale privatisations, but soon proceeded with one of the most radical and fast state-enterprise reforms ever experienced in Latin America. Fujimori emphasised in December 1990 the need to maintain “strategic enterprises”, such as those that deal with telecommunications, petroleum, water and electricity, under state ownership. However, in October 1991 Economy Minister Carlos Boloña signalled a clear change in government’s views on privatisation, as he stated that Peru was willing to privatise, not only “strategic enterprises” like mining and petroleum, but also social security, pension funds, education and health. [100]

Privatisation program was one of the structural reforms the government undertook in the beginning of the 1990s. The reforms were aimed at promoting market-based competition and free international trade, more flexible labour market, at liberalising the financial system, eliminating price controls and implementing sector reforms for the deregulation of markets. According to Torero, all these reforms were complementary and necessary to the privatisation program. By doing these reforms, the government “recognized that adequate regulatory and institutional frameworks and a competitive market for the product, and not just ownership, were determining factors in the success of the privatization process”. [101] According to the Bank, progress on institutional reforms in Peru was substantial in early 1990s. Peru succeeded in dismantling of a myriad of government agencies, such as development banks and state owned enterprises. Institution development progressed as Peruvian government revamped or created some “technically efficient and politically autonomous agencies”, for example the Central Bank, the tax collection agency (SUNAT) the customs agency (SUNAD), the competition supervision agency (INDECOPI) and the agency in charge of privatisation (COPRI).[102]

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[99] Teivainen (2002). 112-121
[100] Teivainen (2000), 9-10
[101] Torero (2003)
[102] Peru Country Assistance Evaluation 2002, 18

According to Torero, the state-owned enterprises in Peru in the beginning of the 1990s were characterised by inefficient provision of goods and services, ambiguous objectives, extensive intervention by politicians, decapitalisation of investment resources and a lack of fresh investment resources. The state enterprises registered accumulated losses of more than US$4 billion in 1989-1990. In order to improve the situation the Peruvian government designed, with the World Bank, normative and institutional framework in order to promote private investment as the main vehicle of economic growth. One of the key aspects of this new framework was a program to privatise public enterprises in 1991. The privatisation process was started in February 1991, with the enactment of Supreme Decree 041 that limited the State to managing 23 companies. Private investments, both domestic and foreign, were encouraged. The government established the Commission for the Promotion of Private Investment (COPRI) to manage the overall privatisation process and the Special Privatisation Committees (CEPRIs), which were in charge of the planning and execution of individual privatisation processes. [103]

Various laws were instituted in order to facilitate the privatisation process. One of the most important laws, according to Torero, was Law of Foreign Investment Promotion, which mandated equal treatment of national and foreign capital. State was also authorised to grant the guarantees and safeties necessary to protect foreign acquisitions and investments. Foreign investors were also granted facilities for the payment of taxes and debts owed by state enterprises in the privatisation process. In 1993, all of these reforms were written into law with the approval of the new Constitution, which included the promotion of free private initiative and equality between national and foreign activities, the encouragement of competition and equal treatment for all economic activities and the guarantee of the possibility of the signing of Stability Agreements between private investors and the State. In addition, the State subscribed to many International Agreements for the protection of foreign investment and conflict solution through international arbiters. [104]

The main objective of the privatisation process was to privatise as many public companies as quickly as possible. The most common practise for privatisation in Peru

[103] Torero (2003)
[104] Torero (2003)

was public auction. In 1991 two public companies were privatised. In 1992, ten companies were privatised drawing in revenues of US$706 million in projected investment. In 1993, 13 companies were sold for a total of US$317 million and projected investment of US$589 million. In 1994, the government sold its natural monopolies in the telecommunications and electricity sectors, which resulted in US$2,579 million in revenues collected and US$2,050 million of projected investments. In 1995 and 1996, 64 companies were privatised, producing revenue of US$3,370 million and investment commitments of US$2,765 million. In 1997 still 25 companies were sold for US$447 million and projected investment of US$706 million. Most of the privatisation process occurred in the telecommunications, electricity, finance, mining and hydrocarbons sectors. However, by 2003, there were virtually no private participation in the transportation, water or sanitation sectors and little in agriculture. Telecommunications, electricity and financial services accounted for 80 percent of the total revenue collected during the privatisation process.[105]

In December 1996 law established the Commission for the Promotion of Private Concessions (Promcepri). This public agency is in charge of evaluating and awarding concessions to the private sector for the provision of public services and infrastructure. Sectors covered by the concessions were electricity, petroleum processing and distribution, the construction and operation of tourism facilities, highways, railways, forestry management, sea and airports, and telecommunication licenses.[106] The World Bank has stated that the program was by 1997 “remarkable”. Only major complaint the Bank had at that time was the government's unwillingness to privatise the public water company, *Sedapal.* [107]

In 1998, the privatisation process “made way” for the concessionary process of transportation infrastructure. CEPRIs were created for the concession of for example airports, ports, road networks and mobile telephone bands. The revenues collected through privatisation slowed down since 1997. According to Torero, this slowdown is attributable to both domestic and foreign factors, such as the Russian crisis, El Niño, the Peruvian political crisis and others.[108] At the end of the decade the World Bank

[105] Torero (2003)
[106] www.imf.org/external/np/loi/050598.HTM
[107] Teivainen (2000), 11
[108] Torero (2003)

curtailed and postponed social investment projects because the government halted the privatisation program. Institutional components of several World Bank projects were delayed or cancelled because of governments unwillingness to carry out reforms such as decentralisation and further reform of the state. [109] The World Bank sees the privatisation process to be so essential to Peru's development, that it has 'punished' Peru by postponing social investment loans.

By the year 2001, the privatisation process in Peru had involved 252 transactions, including 42 state owned enterprises, brought US$ 9.2 billion in revenue to the Treasury and mobilised an additional US$ 11.4 billion in new investments. However, the success in attracting private participation and capital focused on a few sectors such as telecommunications, electricity, banking, hydrocarbons and mining. [110]

The Country Assistance Strategy in 2002 states that the Peruvian government wants to foster larger private sector participation in ports, remaining areas of electricity generation and distribution, in selected water supply and sanitation systems and in the highway sector. The government aims to increase the private sector participation in order to improve efficiency of management of these sectors and to attract private sector investment to expand services. [111]

In social services sector, private pension system was created at the end of 1992 and the system of pension fund institutions was inaugurated in mid-1993.[112] Peru was the second country in the world to privatise pension system, after Chile, which had privatised in 1981. There are three ways in which pension privatisation have been done in Latin America. By replacing the public pension system with private ones, mixed system with both public and private pension systems and the way it was done in Peru, two competing pension programs between which the workers have to choose which to participate in.[113] Private investment is also encouraged in education and health. In 1997 the government issued a new law, which allowed private companies to provide health

[109] Peru Country Assistance Evaluation 2002, 18
[110] Torero (2003)
[111] PERU CAS 2002-2006, 13
[112] Teivainen (2002), 130
[113] Turner (2005)

services (EPS) within the social security system. Also a regulatory body, the Superintendency of Health Services Providers, was established.[114]

The World Bank aims to extend the privatisation process in Peru to new sectors. In 2002-2006 country assistance strategy the Bank plans to make an assessment of strategies for private sector participation in water and sanitation. [115]

[114] www.imf.org/external/np/loi/050598.HTM
[115] PERU CAS 2002-2006, 24

4. THE EFFECTS OF PRIVATISATION ON DEVELOPMENT

There are various different perspectives from which the effects of privatisation on development can be valued. I will use the Bank's own objectives of privatisation and first study the economic and fiscal objectives and consequences of privatisation and then social and political objectives and consequences. Obviously it is sometimes impossible to see which economic or social consequences were the results of privatisation or maybe some other cause as there are many factors interacting in society. However, as the Bank believes that privatisation has an impact on development, I will also believe that this impact can be found and studied. Perhaps the easiest way to view the impacts would be to study a privatised company. There have been studies calculating the firm performance before and after privatisation. Problem here is that as the world around the company has changed, there could have been some changes in the performance even if it had not been privatised. Also a study of a one company does not give very good picture of the development of a whole society, which is what I am interested in. In addition to the economic performance and economic development, I will also examine the more indirect effects, social effects such as changes in employment, equality and poverty. In other words, I will try to examine how the privatisation process has effected the overall development of Peru in the 1990s.

4.1 Privatisation and Economic Development

I will discuss the effects of privatisation on social development in the next chapter. First I am going to focus on the effects that privatisation has had on economic development in Peru in the 1990s. As mentioned in the previous chapter, the World Bank's stated economic objectives of privatisation include economic growth, improving the overall efficiency of the economy, improving the efficiency, productivity and profitability of firms, improving the quality of products and services, and attracting foreign investment. Fiscal objectives are reduction of government subsidies to public enterprises, raising money from the sale of state-owned enterprises and increasing tax revenue from private enterprises.

According to liberal theory, privatisation is expected to lead to greater efficiency and to more rational pricing policies, because the private sector is motivated by profits. The public utilities often keep prices under the operational costs and they aren't usually very efficient in collecting fees from customers, which adds to their losses. [116] Governments often use public enterprises for non-commercial objectives, which in many cases has led to over-staffed and badly managed companies. Public enterprises often cause substantial fiscal deficits and thus, private participation can have many positive fiscal impacts. Improvement of financial self-sustainability of utilities reduces the need for subsidies, which are often large in public enterprises. By passing responsibility for financing of utilities from taxpayers to users, governments can reorient their expenditure towards the social sectors, like health and education. Privatisation can also increase the government's opportunities to raise revenues through divestiture proceeds and license or concession fees. [117]

Infrastructure privatisation has been important, because according to World Bank, modern energy, telecommunications, transport and water services play an important role in economic growth[118]. Infrastructure has traditionally been a responsibility of the state, but in recent decades governments in developed as well as developing countries have had difficulties in meeting the growing demand of these services. Privatisation was seen as a way of reducing the fiscal burden that the provision of infrastructure and industry was making on government budgets. In addition to finance, private participation was also expected to bring expertise to privatised companies. [119]

These are the economic reasons why the World Bank encourages governments to increase private participation in various sectors. One additional reason is that revenue collected from privatisation can be used to pay off foreign debt. This will help the country to get credit worthiness and attract more investment.

[116] Harris (2003), 5
[117] Harris (2003), 20, 23
[118] Miller-Adams (1997), 34
[119] Harris (2003), 3, 17

4.2 Privatisation and economic development in Peru in the 1990s

There have been many praises for the privatisation process of Peru. Torero states that Peru's privatisation process was rated one of the early success stories of privatisation in Latin America [120]. The Bank considers the reforms - privatisation process as one of them - made in Peru in the early 1990s as "one of the most radical and successful in the world". This is proved by the fact that inflation declined, investor confidence recovered and economic growth resumed. The Bank considers that it was efficient in promoting the economic reforms in Peru. After the first goals of macroeconomic stabilisation and implementation of first-generation structural reforms were achieved, the Bank started pursuing its main goals in 1993-1994. These goals were poverty alleviation, infrastructure development, macroeconomic sustainability and institution building. The Bank sees itself as succeeding in achieving most of these goals. Economic growth was high, investment grew, the budget deficit was eliminated and inflation kept reducing. [121] The World Bank's Second Social Development and Compensation Fund (FONCODES) Project Staff Appraisal Report states that the economic reforms of the Fujimori government in 1990 brought about a remarkable social and economic recovery in Peru. Inflation was reduced from 7600 percent in 1990 to 10 percent in 1995. As encouraging as these results are, the economic recovery had in 1995 succeeded only in bringing the per capita GDP back to its 1965 level. [122]

I will start the closer assessment of economic development with the economic growth, as it often is the first development indicator mentioned in the Bank texts, and the Bank sees it as a prerequisite in achieving social development and poverty reduction. In Peru, economy grew after the privatisation process started in 1991. The economic growth of the 1990s, however, needs to be compared to the 1980s, which was not a particularly good decade for Peru when measured with gross domestic product (GDP). The real growth rate between 1980 – 1989 was only 0.6 percent. Annual average growth of GDP in Peru was –0,7% in 1980-84 and 2,6% in 1984-87. [123] There were some good years in the 1980s, as the real growth rate between 1986 and 1987 was 5.9 percent. [124] Average

[120] Torero (2003)
[121] Peru Country Assistance Evaluation, 17
[122] FONCODES Staff Appraisal Report 1996, 1.1 and 1.2
[123] Third World Economic Handbook (1989), 54
[124] The World Bank Atlas 1988, 8

annual growth in per capita consumption was –3,7% in 1980-84 and 4,7% in 1984-87.[125] However, the GNP per capita then rapidly fell in 1989, the real growth rate between 1987 and 1989 coming down to –11.2 percent.[126]

In practice, Peru had started to come closer to the development path advanced by the World Bank in 1988 when president García's 'rebellion' against the International Monetary Fund failed. In late 1990, after inauguration of President Alberto Fujimori, the government introduced fiscal austerity measures advocated by the Bank and the IMF. This seemed to have a short-term negative impact on economic growth. In 1991, when the privatisation process started, the per capita income had dropped to its lowest in 30 years[127]. However, the economic growth after the somewhat bitter start of Fujimori government picked up, and average annual real growth of GNP per capita was 4.6 percent between 1990 and 1997.[128].

Peru experienced an economic slowdown between 1997 and 2001. According to World Bank Country Assistance Evaluation the Peruvian economy grew at 3.8 percent between 1991 and 2001, which means 2 percent growth per capita. Growth between 1991 and 1997 was 5.7 percent but only 0.9 percent during 1997 – 2001. Economic growth, which the Bank considers to be necessary for reducing poverty and achieving social development, has been achieved during the decade. However, according to the Bank, the growth was not enough as it was "insufficient to have an impact on the extent of poverty". [129]

In the 1995 World Bank Atlas purchasing power parity (PPP) was added to development indicators. In The World Bank Atlas 1998, the Bank started to rank countries on both GNP per capita and PPP per capita, which uses international comparisons of average price levels. The GNP per capita converts national currencies into dollars at prevailing exchange rates and PPP into international dollars that would buy the same amount of goods and services in a country's domestic market as $ 1 would buy in the United States. It is often said that the PPP gives a better picture of the

[125] Third World Economic Handbook (1989), 54
[126] The World Bank Atlas 1990, 8
[127] Torero (2003)
[128] The World Bank Atlas 1999, 36
[129] Peru Country Assistance Evaluation 2002, 16

peoples' incomes, because it takes into account the fact that you can buy very different amounts of goods for one dollar in different countries. In 1996, Peru was 59th on GNP ranking and 70th on PPP ranking. Both of its rankings declined and in 2000 Peru was ranked 100th on GNP per capita and 111th on PPP per capita. This ranking only tells us how well Peru did in comparison to other countries and not how well it had done in comparison to previous years. Although GNP per capita did fall from $ 2,420 in 1996 to 2,080 in 2000, the PPP per capita went up a little from 4,410 to 4,660[130]

To sum up, the economic growth was quite well in the 1990s in Peru. Despite the economic slow down after 1997, per capita income doubled between 1991 and 2001 and according to the purchasing power parity, the real incomes in average bettered as well. In addition to economic growth, there are other indicators of economic development. The Bank is interested for example in investments, debt ratio, exports and firm performance as indicators of economic development.

Maximó Torero has studied firm performance in Peru after privatisation. His study included 47 percent of the companies involved in the privatisation process and 86 percent of the total value of transactions undertaken. Three major privatised sectors were studied, and those are telecommunications, electricity and the financial sector. Firm performance was measured by profitability, operating efficiency, capital expenditures, output, employment and leverage. According to his study, the performance indicators of the privatised companies showed a significant improvement after privatisation. Three basic indicators: sales, cost per unit and labour, show that privatised firms significantly increased their sales compared to firms still state-owned. There was also a significant reduction in cost per unit.[131]

However, at the end of the decade the financial performance of the privatised telephone company and the electric utilities declined. Torero guesses that the unsatisfactory results of the electricity sector could be a consequence of the incomplete privatisation process in the sector, as one of the major generating enterprises and all of the distribution enterprises in the south were still not privatised in 2003. Although in the late 1990s there was a decrease in performance in the newly privatised enterprises, which implies

[130] figures for 1996 are from The World Bank Atlas 1998 and figures for 2000 are from The World Bank Atlas 2002
[131] Torero (2003)

less profits, Torero feels that this “could have been the result of an increase in competition in the sector and a slowdown in services such as electricity due to the privatisation process”. In the financial sector there was no significant impact on profitability measures and leverage indicators, but there was a significant increase in the operating efficiency and coverage of the privatised banks. The increase in operating efficiency is, according to Torero, mainly explained by the 50 percent reduction in employment. However, Torero sees the overall effect of privatisation on performance as positive and urges the process to continue.[132]

One of the major criticisms of the privatisation process is that a significant reduction in the number of employees could be the major reason for the improvement in performance, rather than a real increase in total factor productivity. However, Torero argues that there is no significant difference between the post-privatisation performance indicators and the post-privatisation performance indicators under the assumption that there were no layoffs.[133]

One of the Bank’s stated goals for privatisation is to obtain higher levels of domestic savings and investment, and attract and provide opportunities for foreign investors. The share of private investment did grow in Peru from 16 percent of GDP in 1991 [134] to 24 percent in 1998 [135].

> “The reforms of the early 90s, in which the Bank played a significant role, totally altered the environment for private sector development and set off rapid private investment growth. As the decade progressed, two primary obstacles to private investment, the unpredictability of the judiciary and tax instability, became more pronounced and, together with growing political tension, put a damper on private investment after 1997.”[136]

[132] Torero (2003)
[133] Torero (2003)
[134] The World Bank Atlas 1994, 19
[135] The World Bank Atlas 2000, 43
[136] Peru Country Assistance Evaluation 2002, 20

The foreign direct investment figures can be found in the World Bank Atlas since 1995. Foreign direct investment was 3.3 percent of GNP in 1995[137], 3.8 percent in 1999[138] and fell to 1.3 percent in 2000[139]. For example in the telecommunications sector, the privatisation has attracted foreign investors in Peru.[140]

Foreign debt has been a problem for many developing countries since the debt crisis started in 1982. Peru had problems with managing its debt in the 1980s, which resulted in exclusion in the international markets. The World Bank sees the unmanaged debts as a barrier for development, because it uncourages investors. Minister Carlos Boloña said in 1991 that the income that would be gathered through privatisations could be used for paying the foreign debt. The connection between the debt payments and privatisation was clear even before that. Debt was a principal reason for the financial problems of the state and privatisation money helped the situation temporarily. Over the years more direct mechanisms were also established to connect the debt issue with the privatisation. For example, the direct exchange of foreign debt titles into shares in privatised state-owned enterprises was initiated in October 1994. [141] The Bank states that Peru has many competitiveness problems, such as frequent economic policy changes and high indebtedness in the corporate sector. Peru's formal private sector became highly indebted during the first years of the 1990s and many companies had difficulties in paying the debt after the slowdown of the economy in 1997. These competitiveness problems are reflected in low levels of exports compared to other Latin American countries. In 2001, Peru had an export to GDP ratio of 16 percent, which was lower than other Latin American countries, for example Chile (35%), Ecuador (34%) and Bolivia (19%). [142]

However, there has been improvement over the decade, as the export ratio to GDP was 8 percent in 1991[143] in Peru and 9 percent in 1994[144]. The World Bank did criticise Peru in the beginning of the 1990s for having too small export sector and said it ought to be developed rapidly in order to become an 'engine of growth'. According to the Bank,

[137] The World Bank Atlas 1997, 57
[138] The World Bank Atlas 2001, 59
[139] The World Bank Atlas 2002, 61
[140] Evaluation of Diesel Power Plants in Four Countries, Peru, 2001
[141] Teivainen (2000), 10
[142] PERU CAS 2002-2006, 10
[143] 25th World Bank Atlas (1992)

opening up the economy will do this naturally. [145] In the beginning of the 1990s, Peru had a small, strong export-oriented private sector in mining and fishing, and textiles and garments were the only manufacturing sectors where the private sector was significantly export-oriented.[146]

There has been economic growth in Peru in the 1990s after privatisation, just as the Bank has anticipated. The Bank argues that privatisation promotes economic growth, which in turn reduces poverty and improves the standard of living. However, there are competing views, which suggest that the economic development: growth and increased efficiency, in Peru in the 1990s could have happened without privatisation as well or that some economic consequences which the Bank sees as promoting development are actually deterring development. There are also views that economic growth, when it does happen, does not necessarily reduce poverty, but I will examine this view in the next chapter.

SAPRI report argues that the effects of privatisation often vary depending on the type of enterprise. There are also differences when assessing impacts from a microeconomic or macroeconomic perspective. The SAPRI report has found many positive impacts in privatisation of small businesses in general. For example, it can create a viable entrepreneur stratum, and these small firms are very important in local employment generation and in meeting local needs. The efficiency of these small businesses can also increase if management has been transferred to the local level. However, it may be hard for these small enterprises to compete with the larger, often foreign owned shopping centres. The privatisation of industrial enterprises has been the backbone of the process of dismantling state ownership in a number of countries, including Peru. The impacts of the privatisation of industrial enterprises have been quite mixed. However, the results depend on many factors, not only on the mode of ownership. For example, the inefficient management, the scarcity and misuse of credit and the lack of technological and marketing support affect the results of the privatised enterprise. [147] The SAPRI Report claims that there is no clear evidence, that the form of ownership determines the level of efficiency of the company or that privatisation in itself leads to better

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[144] World Bank Atlas 1996, 19
[145] World Bank, Peru Private Sector Assessment (1994), 24
[146] World Bank, Peru Private Sector Assessment (1994), 12
[147] Structural Adjustment, The SAPRI Report (2004), 114-115

efficiency. At the macroeconomic level the rate of economic growth (real rate of GDP) can be taken as an indicator of efficiency. In the countries studied in the SAPRI Report, there was no sign of any general acceleration of growth following the period of privatisation, which started in the 1980s. Report adds that even in the countries where the economic growth did happen, the growth did not benefit the whole society but only a limited group of people. [148]

One of the Bank's reasons to recommend privatisation is that it attracts foreign investment to the country. But there can also be a downside in foreign investment. In many countries the principal beneficiaries of the privatisation programme have been foreigners, especially multinational corporations and other large companies, who have obtained high percentage of the total divestiture proceeds. SAPRI report argues that while a certain amount of foreign ownership in the industrial and service sectors is advantageous for a developing country because it brings in more advanced technology, knowledge and new products, foreign influence may also cause much uncertainty and difficulties. The dominance of foreign capital often obstructs the development of local industries or crowds out existing ones. Foreign companies can be volatile, as they seek higher profits from lower labour costs, and might decide to relocate at any time, laying off employees and causing serious problems at the local level. At the macroeconomic level, the repatriation of profits or the withdrawal of capital can cause current-account problems and, in the worst of cases, destabilise the local currency. The general problem with the dominance of foreign ownership is that decisions that affect the lives of local people are taken out of the control of local societies. [149] The major part of the privatised state-owned enterprises in Peru have been transferred to foreign ownership and the government, much less the people of Peru have little to say about the way these companies are run. Also the overall lack of regulation of the privatisation process has been criticised. [150]

In many countries, and Peru is no exception, governments have used revenues from privatisation to pay off public debt. Birdsall and Nellis argue, that although that often does make sense in a highly debt-ridden country, the use of privatisation revenues is a

[148] Structural Adjustment, The SAPRI Report (2004), 120
[149] Structural Adjustment, The SAPRI Report (2004), 121-122
[150] Teivainen (2000), 10-11

function of the overall fiscal performance of a government, since even when revenues reduce debt stock, indiscipline of the fiscal side means those revenues are indirectly financing the government's current expenditures or increasing its changes to borrow more.[151] It can also be argued that the revenues from privatisation should be used in investments in Peru, for example in infrastructure, education or health. Teivainen argues that the fact that Peru pays its debt more obediently than in the past means inadequate nutrition, education and health care for many Peruvians[152].

Although economic growth has happened after privatisation, there are views that the good performance is not necessary a result of privatisation as such, but other reforms, such as increased competition. Joseph Stiglitz argues that state monopolies do not contribute to economic development, because they stifle competition. However, the reason why the Washington consensus focused on privatisation was not concern over lack of competition but focus on profit incentives. This made perfect sense, according to Stiglitz, because the state enterprises were inefficient and their losses contributed to the government's budget deficit, leading to macroeconomic instability. Thus privatisation would both improve economic efficiency and reduce fiscal deficits. The transfer of property rights to new owners would lead to profit-maximising behaviour that would eliminate waste and inefficiency. Budget deficit would be financed through the revenue collected from the sale of state enterprises.[153]

Stiglitz argues that the case of China and Russia has demonstrated that it is competition rather than the form of ownership, which is important in economic development. China has not privatised but has extended the scope of competition whereas Russia has privatised without doing much to promote competition. The contrast in performance is significant as China has managed to sustain double-digit economic growth for two decades and Russia's output is below the levels attained more than a decade ago. However, Stiglitz still argues that the Washington consensus is right in promoting privatisation, because governments should devote their resources to areas the private sector does not enter.[154] However, although a proponent of privatisation Stiglitz criticises the way in which privatisation was done in many countries, including Peru.

[151] Birdsall & Nellis (2002), 23
[152] Teivainen (1999), 91
[153] Stiglitz (1998), 20
[154] Stiglitz (1998), 22-23

According to the IMF and the Bank, privatisation was to be done as quickly as possible. Stiglitz says that before privatisation, competition and regulation legislation should be created, and not the other way around.[155]

Torero also stresses the importance of complementary policies of privatisation. Together with the privatisation program, the government of Peru undertook a set of structural reforms, which were complementary and necessary to the privatisation process. Torero argues that in so doing, "the government recognized that adequate regulatory and institutional frameworks and a competitive market for the product, and not just ownership, were determining factors in the success of the privatization process."[156]

As a conclusion from Stiglitz and Torero, it can be argued that privatisation is important in achieving economic growth, just as the Bank has argued. Critics, such as SAPRI report, argue that in some countries the privatisation has not resulted in economic growth. However, this is not the case in Peru where the economy crew in the 1990s, even during the economic slowdown since the 1997. Other economic indicators have also improved. Now it is time to view the other part of the Bank's argument: that in addition to promoting economic development, privatisation promotes social and political development as well. The World Bank has stated that the social and political objectives of privatisation are to improve the welfare of society, promote ownership of private enterprises by nationals, create a property-owning middle class, increase employment and reduce corruption and the abuse of public office.

4.3 Privatisation and social development

Privatisation has consequences on social and human development as well as on economic development. Many indicators have been created for measuring social and human development. They range from indicators of material resources, education and health, to poverty and equality indexes. It is also widely recognised that the state of environment has an effect on the quality of life, as well as political freedom and other human rights. The World Bank uses most of the development indicators, which have

[155] Stiglitz (2004), 91-94
[156] Torero (2003)

been invented, some more consistently than others. Of course the problem with human life is that many of its aspects are very difficult to express with numbers. Even those aspects that can be quantified, the gathering of data is costly and difficult. For the World Bank, the poverty index is the most important indicator of development, which is why I will concentrate on that as well.

The debt crisis of the early 1980s made it increasingly difficult for developing country governments to finance their wide range of companies. As a consequence of lack of financing, public companies were often unable to meet increasing demand and extending services to the poor.[157] World Bank argues that well designed privatisation schemes can bring about substantial increases in overall welfare of society. Main sources of these welfare benefits are increased investment to bring services to new consumers, lower prices, and improved productivity and efficiency. The technical and managerial competence of the private sector, and it's more sustainable pricing policies and better financial discipline provide more resources for investing in expansion of services.[158] Important reason for privatisation is that it leads to greater competition and higher levels of growth. Economic growth is believed to benefit all members of society, rich as well as the poor. [159] Privatisation, according to the Bank, will decrease poverty through economic growth and by giving the poor better access to services, such as health care, education and infrastructure. According to the neoliberal theory the privatisation should also increase national employment as a consequence of attracting foreign direct investment and improvement in overall efficiency of the economy. One of the objectives of privatisation advocated by the World Bank in various countries was to create more jobs. The Bank also argues that privatisation will enhance development through the reduction of corruption. [160]

Next I will study the effect of privatisation to different aspects of human and social development in Peru in the 1990s. I will focus on corruption, the changes in employment and on the effects of privatisation on the poor.

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[157] Harris (2003), 4
[158] Harris (2003), 17
[159] Miller-Adams (1997), 36
[160] The Structural Adjustment, the SAPRI Report (2004), 122-124

4.3.1 Corruption

Corruption means the misuse of public funds and resources, and using public office for ones own benefit. Thus corruption violates the principle of equality and justice. Corruption leads to unequal distribution of public resources, which offends the equality of citizens, distorts the economical and political structure of society and diminishes the credibility of political leaders. [161] Corruption can also make public policies ineffective.[162]

One of the problems of public enterprises, and thus a reason for privatisation, is corruption. Because the public enterprises in developing countries are often unable to serve all potential clients, employees and government officials have an opportunity to solicit bribes from customers who are trying to get better access to services.[163] Corruption is seen as a barrier to development, by the World Bank and many development researchers and organisations. According to Susan Rose-Ackerman, corruption is a symptom of a poorly functioning state, and that can undermine economic growth. Studies have indicated that strong legal and government institutions and low levels of corruption help foster investment and economic growth. Corruption can also increase inequality, because those who have money and power can have better services. People who pay and receive bribes can expropriate a nation's wealth, leaving little for the poor. Even countries, which have extensive natural resources, may fail to develop in a way that benefits ordinary citizen, if corruption is systematic. Corruption effects the efficiency and equality of economic system and society as a whole.[164]

Rose-Ackerman argues that reforms, which increase the competitiveness and openness of the economy, will reduce corruption. For example, if a subsidy is eliminated, there is no need for anyone to pay bribes in order to get subsidised products, and if the state does not have the authority to restrict exports, no one will need to pay bribes if they

[161] Hellsten (2004), 172-175
[162] Sen (2001), 275
[163] Harris (2003), 3
[164] Rose-Ackerman (1997), 35-37

want to export, and finally, if state owned companies are a centre of corrupt payoffs, privatising these companies will eliminate corruption. [165]
In addition to deterring economic growth, corruption also undermines democracy and good governance, and maintains inequality in society. Corruption increases poverty and prevents the unequal distribution of welfare. [166]

According to the SAPRI report, there are no simple ways of getting rid of corruption, as it often is deeply rooted in a society and privatisation is not a quick answer to the problem. SAPRI Report claims, that privatisation itself is often accompanied by corruption and a lack of transparency. It is believed that privatisation processes were not free from political interference, corruption and underhand dealings in which foreigners and state officials were often the only beneficiaries. [167] Privatisation and the new regulatory institutions can also be corrupted, when bidders bribe privatisation officials.[168] Hellsten goes even further in his critic and argues that market economy and privatisation have led to increasing corruption, both in developed and developing countries. [169]

There are claims that privatisation process in Peru also suffered from corruption. In 2002 the government of Peru decided to sell two electric companies to Belgium's Tractebel for $167 million, but was forced to suspend the sale after violent protests. Tractebel was the only bidder for these companies, which had been profitable under state management. In this case the protesters were not opposed to privatisation as such, but to the "authoritarian way in which the government was carrying out the process" and to the lack of transparency. [170] Nancy Alexander agrees that the privatisation in Peru has not been transparent. Little information has been made public about the privatisation process. Parliament, regulatory bodies or the public have not had an opportunity to scrutinise and weigh in the plans or contract provisions.[171]

[165] Rose-Ackerman (1997), 45-46
[166] Hellsten (2004), 171
[167] The Structural Adjustment, The SAPRI Report (2004), 126-127
[168] Rose-Ackerman (1997), 46
[169] Hellsten (2004), 176
[170] www.worldpress.org/article_model.cfm?article_id=765&dont=yes
[171] Alexander (2004) www.servicesforall.org/htme/worldbank/Peruvians_at_risk.shtml

4.3.2 Social indicators

The welfare of society includes well-being and quality of life of all citizens. The World Bank measures the welfare of society in various indicators of social and human development. Estimated in many World Bank standards, development in Peru in the 1990s has been good. Economy has expanded and several social indicators have improved. However, the most important social development indicator of the Bank, poverty, has not significantly decreased. Other indicators of social and human development used by the Bank include for example population growth, life expectancy at birth, infant mortality rate, child malnutrition, share of female labour force, total fertility, primary and secondary school enrolment and illiteracy rate.

The World Bank has been widely criticised for the social costs of structural adjustment programs since the 1980s. The Bank praises the Fujimori government for recognising the need to ameliorate the social costs of the economic adjustment program of 1990 soon after the program was initiated.[172]According to the Bank's Peru Country Brief, the 1990s was a good decade for the country as the investment in infrastructure and services led to improvements in many social indicators. Infant and maternal mortality diminished significantly as the infant mortality rate dropped from 54 deaths per 1,000 live births in 1990 to 32 in 2000 and maternal mortality decreased from 265 deaths per 1000,000 in 1993 to 185 in 2000. From 1997 to 2001, there was also an important expansion in the access to secondary education. Attendance increased to 74 percent in urban areas and 44 percent in rural areas. [173] Life expectancy in Peru has gone up steadily, from 62 years in 1989 to 69 years in 2000 [174]. Although health indicators have improved, most of them still remain below the average for Peru's income level. [175]

The Bank has stated in many of its publications, that the social development in Peru in the 1990s is a consequence of the economic growth and improved targeting of investments to the poor. However, in Country Assistance Evaluation published in 2002, it is stated that the improvement of various social indicators is the result of innumerable domestic and donor-supported programs and is quite independent of the rate of

[172] FONCODES Staff Appraisal Report 1996, 1.8
[173] www.worldbank.org, Peru Country Brief
[174] The World Bank Atlas 1990, 8 and The World Bank Atlas 2002, 29

economic growth. [176] Peru Country Assistance Evaluation furthermore states that although social indicators have improved through the 1990s,
"It is not possible to estimate the impact of the Bank's program. Social indicators are improving everywhere over the past several years for many reasons, and did so in Peru also during the late 1980s when Peru was in extreme economic crisis and when assistance from multilateral institutions was halted".[177]

So although Peru has improved its social indicators in the 1990s, the Bank can not take it to be only a consequence of Bank programs or loans, or even Bank advocated reforms. The World Bank acknowledges that social development has happened in countries, which have not followed the orthodox economic policies. Social indicators have improved in Peru since the start of the privatisation program, but did improve in the 1980s as well, which was a time of nationalisation, which makes it difficult to assess the impact of privatisation on social development from these social indicators. More straightforward ways of analysing the impact of privatisation on welfare are for example price and availability of services and products, especially for the poor and effects on ownership and employment.

4.3.3 Employment

Birdsall and Menezes argue that key area of reform was missing from the development agenda during the 1990s and that is labour markets. Lack of jobs and low wages are the main concerns of Latin Americans. The share of workers covered by labour regulations and social protection in Latin America is now less than it was in the early 1990s. Job creation has been very weak in the region, and has concentrated mostly in low-productivity activities. During the 1990s, job growth was slower than the growth of working-age population and many countries registered relative increases in the share of jobs considered low quality, such as part time work, temporary employment and self-employment. In every country of the region, a large informal sector, where labour productivity is low and workers lack minimal protection and benefits, persists.[178] In Peru, and many other countries in the region, the efforts to address labour rigidities

[175] PERU CAS 2002-2006, 4
[176] Peru Country Assistance Evaluation 2002, 16
[177] Peru Country Assistance Evaluation 2002, 20

were limited to the introduction of partial reforms such as temporary and fixed-term employment contracts with no benefits or incentives for training. Birdsall and Menezes argue that the results of these partial reforms have been “more distortions and inequalities”. For example, greater wage gap between protected and temporary workers, reduced access and mobility to higher quality jobs by the women, young and unskilled workers. Reforms have not succeeded in generating employment.[179]

The most direct effect of the privatisation on the welfare of citizens is the fact that during the privatisation process many employees of the privatised companies lose their jobs. Usually some lose their jobs before the company is sold, when the company is prepared for the sale and even more people lose their jobs after the privatisation has taken place. This was the case also in Peru, where approximately 76 450 people lost their jobs during privatisation process and only 36 percent of the employees of privatised companies kept their jobs[180].

In most countries the privatisation of public enterprises has failed to meet the anticipated goal of increasing employment. The laying off of employees has been a major aspect of the reform in many privatised firms. In many cases the privatisation has been costly especially for women**,** as they tend to be the ones with less education and thus form the highest percentage of those laid off by the new owners. Women have also been indirectly affected by the loss of jobs by male household members and the consequent reduction in family earnings. [181]

Torero argues that the negative effect on employment is due to the fact that state-owned enterprises often hired people based on political criteria, rather than because of their skills and education. Torero says that the “impact of privatization on the welfare of displaced public workers has received little attention in the literature” and the issue receives little attention in his own study as well. He says that there was a significant reduction in direct employment compared to the pre-privatisation period. The most important reduction of direct employment took place among blue-collar workers. However, Torero also mentions that until 1991, Peru had a very restrictive and

[178] Birdsall & Menezes (2005), 2
[179] Birdsall & Menezes (2005), 5
[180] Torero (2003)
[181] The Structural Adjustment, The SAPRI Report (2004), 122-124

protective labour legislation, perhaps the most restrictive in Latin America. After the reforms between 1991 and 1995 no other country in the region had so liberalised its labour market and this has also affected the employment levels in the country, which implies that the reduction in employment can not be explained only by privatisation. [182]

Torero argues that although direct employment decreased, the newly privatised companies increased indirect employment. For example in the case of a telecommunications company TdP (*Empresa de Telecomunicaciones del Perú*), contracting service companies created a significant amount of indirect employment and these service companies often hire people who have been laid off because of privatisation. The number of employees in the telecommunications rose from 13,000 employees in 1993 to 34,000 employees in 1998. Torero concludes that there has been increase in indirect employment through services after privatisation and average growth of 28 percent in total employment after privatisation.[183]

Supporters of privatisation argue that only way to get rid of inefficient employers is through privatisation. Stiglizt argues that this is often true, as inefficient state firms are transformed into efficient private ones through reduction of workers. However, he says that the efficiency of the whole economy, not just only one company, should be considered. Critics say that privatised firms don't take into account the social effects of the lay offs. The social costs of unemployment are often severe and influence also others than just the laid off worker and he's or hers family. [184] In developed countries unemployed are usually somehow supported by the state. In developing countries such unemployment benefits rarely exists and unemployment can lead to increasing violence and criminal activity, as well as social and political restlessness. Unemployment also increases the insecurity, also for those who have kept their jobs for now, increased economic burden for those family members who have jobs, and taking children out of school in order to help support the family. [185]

It is difficult to conclude the effect of privatisation on total employment levels in Peru in the 1990s, as the unemployment figures are not very reliable. According to the World

[182] Torero (2003)
[183] Torero (2003)
[184] Stiglitz (2004), 94
[185] Stiglitz (2004), 95

Bank, in 1994, 17 percent of the economically active population in Peru was adequately employed, 74 percent were underemployed and 9 percent unemployed. [186] Teivainen states that according to the Peru's most often used unemployment statistics, 7 percent of the urban population was unemployed in 1996, 42,6 percent were underemployed and 50,4 percent adequately employed. The extent of unofficial sector and the absence of public unemployment benefit system means that the line between being unemployed and doing random odd jobs is often thin.[187] According to the estimates of the Bank, informal sector employs about 50 percent of the work force, which is high, even in Latin American standards[188]. The absence of unemployment benefits also means that people don't have a reason to register as unemployed, which makes the statistics unreliable.

According to Teivainen, unemployment, low wages and bag working conditions have been one of the biggest concerns of citizens during the 1990s. The development model of the Fujimori government could have worsened the situation, as the new investments have been concentrated on mining and oil, and other industries that do not generate new jobs as much as the growing population needs. It is estimated that every year 300 000 new young people enter the labour market. [189]

4.3.4 Poverty and Inequality

Privatisation has also effected lives of the poor and equality of a society. High levels of poverty and inequality are perhaps the best characteristics of a developing country. Poverty reduction is stated as the central objective of the World Bank's involvement in Peru. The strategy is to alleviate poverty with infrastructure development and institution building through investment lending in infrastructure and the social sectors. [190] Essential part of infrastructure development is privatisation of these services. Also in the social sectors the role of government funding has been decreased, for example by creating private pension funds and increasing private investment in education and health.

[186] FONCODES Staff Appraisal Report 1996, 1.2
[187] Teivainen (1999), 96
[188] World Bank, Peru Private Sector Assessment (1994), 23
[189] Teivainen (1999), 96-97

The Bank measures the welfare of society, in addition to social indicators discussed above, with poverty and inequality indicators, of which poverty is the most important indicator of development. According to the Bank, privatisation will increase economic efficiency and economic growth, which in turns reduces poverty [191]. Poverty is essentially lack of income, although the Bank admits that poverty has many other dimensions than just income poverty. Equality for the Bank means that everyone should have access to resources and services which they need to help themselves out of poverty and to better their lives. Equality is thus important in alleviating poverty. If people have equal opportunities they can fulfil their needs. Thus, according to the Bank, privatisation will improve equality in a society by improving access to services and resources. The Bank sees equality more on terms of equal opportunities, than with equal sharing of the incomes or goods.

The World Bank conducted a research with the United Kingdom Department for International Development about poverty in Peru. The “Voices of the Poor” was designed to collect information about the poor and their lives. Poverty was experienced and described by the poor as multidimensional, including unemployment and underemployment, lack of power over market conditions, small farms’ dependency and vulnerability, high cost of falling ill, deficient educational services, discriminatory and corrupt practices of public institutions, limited access to justice and formal credit, difficulties in securing arable land and rights of tenure, lack of safety and security, domestic violence, discriminatory gender roles and frustrated youth. [192] Despite this recognised multidimensionality of poverty, when defining who are poor, only thing that is taken into account is the income of a person or a household.

In the various papers and studies on Peru, the Bank does not use its own definition of poverty, the ‘people who live under $1 or $2 a day’. Instead it uses the national poverty line. In this definition a household is poor if per capita consumption is lower than the cost of a minimum basket of goods and services. Extremely poor are those, whose level of consumption is lower than the cost of a minimum basket of food necessary to maintain adequate caloric intake. There was reduction in poverty in Peru between 1991

[190] FONCODES Staff Appraisal Report 1996, 1.13
[191] Miller-Adams (1997), 36
[192] PERU CAS 2002-2006, 4

and 1994. The Bank, however, argues that the reduction in poverty did not benefit all of the poor to the same extent, as the poverty declined by 10 percent in Lima, by 6 percent in rest of the urban coast and 12 percent in the urban Sierra, but the reduction was only 4 percent in the rural Sierra. Most of the poor live in rural areas, where in 1994 almost 66 percent of the people were poor. In 1994, almost 50 percent of Peruvians were classified as poor and 20 percent of the Peruvians were extremely poor.[193] In 1991 the rate of extreme poverty had been 23 percent [194].

According to Bank publication in 1996, poverty was expected to decline to 33.4 percent in 2000, and extreme poverty to 9.8 percent. [195] These estimates proved to be too optimistic. Between 1997 and 2001, the percentage of Peruvians living in poverty increased to 54.8 percent, while extreme poverty reached 24.4 percent of the population. [196] Increase was from 49 percent of people living under the national poverty line in 1997. There was still more poverty in the rural areas, where the percent was 64.7 compared to urban 40.4 percent. In 1996 15.5 percent of population were living with less than $1 a day. [197]

Poverty continues to be concentrated in rural areas, where poverty rates are much higher than those of urban areas, and the rate of extreme poverty was five times as high still in 2001. The poverty rate varies between the regions as well. In the Coast the poverty rate was 39.3 percent in 2001, the poverty in Lima was 31.9 percent, in urban areas 44.6 and 62.7 in rural areas. In the *Selva* (jungle), where urban poverty was 62.4 percent and rural 74, the overall poverty rate of the region was 72 percent. It was little lower in *Sierra* (highlands), 68.7 percent, from which the urban poverty rate was 51.6 and rural as high as 83.4. More than half of the extremely poor live in the rural *Sierra,* although it has less than a quarter of the national population. The average net rural household income is $1.30 a day, while in the Peru as a whole it is $3.10. [198] In conclusion, the rate of extreme poverty was higher in 2001 than it was in 1991, and poverty rate was roughly the same.

[193] FONCODES Staff Appraisal Report 1996, 1.3
[194] www.whiteband.org/specialIssues/UNP5/unp52/gcapnews.2005-09-12.150672933
[195] FONCODES Staff Appraisal Report 1996, 1.10
[196] web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/LACEXT/PERUEXT…
[197] The World Bank Atlas 2003, 57

Inequality in a society is a deterrent for development in various ways. There is evidence that inequality can and does hinder economic growth, especially in a country where institutions and markets are weak, like in most developing countries.[199] Unequal society does not offer education, health care and other basic services to the poor, which means that they and their offspring are likely to stay poor in the future as well. For the World Bank, equity basically means that everyone should have access to quality education, health, culture and basic services [200].

One way of examining the welfare impact of privatisation is to study how well the privatised services are available for citizens, and especially to the poor. Here good indicators are coverage of a service and costs of obtaining a service. In Peru in general, coverage has usually increased after privatisation, and the prices have increased in some sectors and decreased in others. For the World Bank the question of access is important, because it is a question of equality. Equal access to basic services is one of the main ways in which poverty can be reduced, according to the Bank. For example, when a household obtains water and electricity, it is more likely to be healthier and better educated than before, and healthy and educated people have better earning opportunities and thus, have better changes of not being poor.

The World Bank sees that education is one of the most important factors in helping people to rise from poverty. Access to primary education in Peru has been widespread, and the attendance level was over 90 percent in 2001, for both poor and non-poor students. Universal attendance at the primary level, one of the United Nations Millennium Development Goals, has thus essentially been achieved. However, the quality of education and the outcomes are poor and children in Peru perform poorly on standardised tests. Rural children perform more poorly than urban, and Bank states that the rural schools are suffering from inadequate learning materials and low teacher quality and motivation.[201]

Torero concludes in his study on firm performance after privatisation in Peru, that in order to assess the influence of privatisation, not only economic efficiency, but also

[198] PERU CAS 2002-2006, 3
[199] Birdsall & Nellis (2002), 2
[200] PERU CAS 2002-2006, 23
[201] PERU CAS 2002-2006, 3,5

service quality and consumer benefits must be taken into consideration. Despite the positive improvement in firm performance after the privatisation, the positive welfare impacts on consumers were not very significant, according to Torero, or were even negative in some sectors, such as electricity. The consumers therefore are not experiencing an increase in welfare, according to him. Telephony is one sector, which has experienced the most significant improvements. However, a significant reduction in household consumer surplus has occurred since 1997. [202]

In telecommunications, the number of phones per 100 inhabitants grew from 2.9 in 1993 to 7.8 in 1998. Also the number of cellular phones grew from 50,000 to 735,000 in the same period. [203] However, there were still 70,000 villages without access to a telephone in 2000, and the penetration of telephone services is still relatively low compared to levels prevailing in the region.[204] In the electricity sector, the coefficient of electrification grew an average of 27 percent and the generation of electricity grew an average of 25 percent after privatisation. [205] In 2000 the Ministry of Energy and Mines estimated that 73 percent of the population of Peru had access to electricity service. However, there are great differences between regions. In the capital Lima, 99 percent of population have access, whereas in the rural areas only around 20 percent of the population have access to electricity. Increase in electricity after privatisation has been “exceptional but uneven”. The overall national coverage increased between 1993 and 2000 from 55 percent to 70 percent, but the rural coverage was still below 25 percent in 2000. According to the report Evaluation of Diesel Power Plants made in Peru, the reasons for low electricity coverage in rural areas are well known. The payment capacity of the inhabitants is low and electricity provision to rural areas is costly because systems are small and users widely scattered. [206]

Because the private sector is unwilling to do these investments, it is still left for the public sector. The public sector invested US$361 million in rural electricity between 1993 and 1998, which increased the rural coverage by about 2 million people[207]. This example shows that the private sector is unwilling to do investments, which would help

[202] Torero (2003)
[203] Torero (2003)
[204] Evaluation of Diesel Power Plants in Four Counties Peru (2001), 43
[205] Torero (2003)
[206] Evaluation of Diesel Power Plants in Four Countries Peru, (2001), 41-42, 51

development, if these investments are not cost-effective. When the costs are high in increasing electricity coverage in some rough mountain area, and there are only a few prospective consumers, it does not make sense for the private sector to invest.

The returns from serving new customers are critical, and prices will have to reflect the costs of expansion. Where revenues from consumers are not sufficient and affordability concerns exists, subsidy schemes could be employed by the government to supplement user fees and extend infrastructure services to rural areas and to the poor.[208] The World Bank also recommends that Peru should promote investments by private sector, municipalities and non-governmental organisation to improve coverage of electricity. Central government should not be an operator but a policy maker, co-ordinator, investment promoter and residual investor. [209]

Nancy Birdsall and John Nellis argue in their study on distributional effects of privatisation, that even when the services after privatisation are expanded to new areas which have previously been underserved, which are thus probably poorer areas, the people can still have difficulties in taking advantage of the services, if the connecting costs are too high. [210]

The most often found criticism against privatisation is that it is perceived as unfair. Privatisation is said to hurt the poor, and benefiting the already rich and privileged. Many believe that privatisation has a negative effect on the distribution of wealth, income and power. Birdsall and Nellis underline, that there can be no simple prediction about the distributional effects of privatisation and in the end, the question is an empirical one. It is difficult to generalise the effects across counties and over time.[211] After over ten years of following the Washington Consensus economic reforms, Birdsall and Menezes feel that Latin American countries have not benefited greatly. Economy has grown but at the same time, the proportion of poor, which had declined during the 1990s, has increased since 2000. The benefits of the reforms have not been shared by all. Increased public spending did benefit the poor, but the Washington

[207] Evaluation of Diesel Power Plants in Four Countries Peru, (2001), 51
[208] Harris (2003), 19-20
[209] Evaluation of Diesel Power Plants in Four Countries Peru, (2001),51-52
[210] Birdsall & Nellis (2002), 17
[211] Birdsall & Nellis (2002), 2, 11

consensus reforms as such benefited mostly those all ready well off, without generating jobs. Income inequalities remain high, and have widened in some countries. Public opinion polls show low support by Latin Americans for fiscal austerity, privatisation and other Washington consensus reforms.[212]

Todaro also argues that most studies indicate that privatisation appears to be successful in promoting greater efficiency and higher output. However, the effects of privatisation on income distribution are likely to be to increase the gap between the rich and the poor. The reason for this is that privatised assets are being concentrated in the hands of small groups of local and international elites. For example in Latin America, many sales of former state-owned enterprises were conducted without competitive bidding, often at predetermined concessionary prices. The process enriched small groups of well-connected investors, both domestic and foreign. Some privatisation even merely replaced public monopolies with private monopolies, thus allowing a few individuals to reap the monopoly profits that formerly accrued to the state. [213] Most privatisation programs have paid much more attention on the efficiency gains than enhancing equity. Privatisation has on average, at least initially, worsened wealth distribution and income distribution. The reason for negative effect on wealth distribution is that privatised assets are most likely transferred to the already rich and the negative income distribution effect arises from movements in prices and wages. [214] In economics, the question of equity of distribution is often seen as a trade-off with efficiency or growth. However, according to Birdsall and Nellis, in an economy that is not perfectly effective, there doesn’t need to be such trade-off. This means that it is possible to implement privatisation in a way that increases both economic efficiency and equality.[215]

In Peru, most of the privatised companies were sold by direct sale, which is an efficient way to privatise profitable companies that attract investors. In direct sale, the company is sold to the highest bidder or to the bidder with the best investment plan. Direct sale is seen as a best way of privatisation, in terms of the prospects for the productivity of the company. However, from the equality viewpoint, it is less tempting. When property is sold to the highest bidder, it will go to someone who already has enough initial capital.

[212] Birdsall & Menezes (2005), 1
[213] Todaro (1997), 633
[214] Birdsall & Nellis (2002), 18
[215] Birdsall & Nellis (2002),4-6

This means that the distribution of assets will become very concentrated. But there is also an equalising effect in auction sales, because auction tends to bring the valuation of privatised assets into line with maximum-profit pricing and this has favourable long-term equity effects. Only a small share of companies, however, is sold for effective prices and therefore the prices of most companies privatised in auctions leave plenty of room for the new owners to make quick profits.[216]

For the Bank, inequality mostly means limited access to services. However, inequality is also a wider concept, which includes the disadvantaged position of certain groups, like women and indigenous people, in a society and an unequal distribution on incomes and resources between different groups and classes. There are some comments on the unequal distribution of wealth, and other inequalities in Peru in the World Bank publications. Mostly emphasis is on gender equality, the welfare divide between rural and urban areas and obviously on the poor. In the late 1990s also the situation of indigenous people has had some consideration as well.

The World Bank estimates that the benefits and costs of the reform program, including privatisation, of the early 1990s were unevenly distributed among the Peruvians. Peru's "wealthy benefited from expanded business opportunities, export growth, a rising skill premium and higher-quality services from privatized utilities while low rates and weak enforcement of personal income taxes kept their contribution to the fiscal adjustment effort limited."
"The poor benefited from particularly strong economic growth in the geographical areas and economic sectors where they were employed and from an increase and improvement in the targeting of basic social expenditure, and many gained access for the first time to water, electricity, and telephone services."[217]

But the middle class was heavily burdened according to the Bank.

> "Thousands of middle class members… lost their jobs in the downsizing of the civil service and state-owned-enterprises as well as in import-competing

[216] Honkkila (1997), 21
[217] Peru Country Assistance Evaluation 2002, 23

industries that went bankrupt during the ensuing trade liberalization. They saw their wages stagnate after undergoing a dramatic decline, and suffered from increases in utility prices and a re-direction of government expenditure toward the poor."[218]

One of World Bank's own goals for privatisation was to create a property owning middle class. But many of middle class members lost their livelihood as a result of privatisation; it is hard to imagine that they would be able to increase their property after that. At the end of the decade the government increased public sector wages and pensions and reduced payroll tax. This, according to the Bank, was "untimely" and done only in order to gain middle class support in the upcoming presidential election in 2000 and contributed to "the fiscal dire straits" of the country.[219] According to Birdsall and Menedez, it should be kept in mind that the middle income households in Latin America are really not "middle class" in a western sense, but often rather poor. Health and education levels are quite low as well. For example in Peru during the 1990s, almost 20 percent of children under the age of five in middle-income households were stunted. [220]

The Bank argued in mid-1990s that the living conditions of the Peruvian poor reflect the uneven distribution of the benefits of development. The Bank argued that the situation could be improved by expanding small-scale improvements in the social and economic infrastructure and targeting them to the poor, especially to rural poor. [221] However, the estimates of rural poverty showed little change over the decade. The Bank admits that there are questions about the distribution of growth between smallholders and modern agriculture, which need investigation.[222] The Bank, however, does not investigate this matter any further. The Bank does not use the inequality indicators for example in the World Bank Atlases, which I have used as material, but they are sometimes mentioned in texts or World Development Reports.

[218] Peru Country Assistance Evaluation 2002, 23
[219] Peru Country Assistance Evaluation 2002, 24
[220] Birdsall & Menezes (2005), 3
[221] FONCODES Staff Appraisal Report 1996, 1.7
[222] Peru Country Assistance Evaluation 2002, 20

Inequality of wealth distribution can be measured with for example the Gini coefficient or the decile ratio. [223] The Bank argues that income distribution in Peru did improve in the beginning of the 1990s, but still was worse than the Latin American average. [224]According to figures of UNICEF, there wasn't improvement compered to the 1980s as the lowest 40 percent of households in Peru had 13 percent share of household income in the 1980s and the highest 20 percent share of household income was 52 percent[225]. In the 1990s the share of lowest 40 percent had dropped to 11 percent and the highest 20 percent of Peruvian households earned 53 percent of the total income[226]. The Gini coefficient ratio in Peru was 44.9 in 1994, and had increased to 46 in 1998. Measured with Gini coefficient the income equality is slightly better than the Latin American average, 51 in the beginning of the decade and 52,6 in 1998.[227] The situation worsened at the end of the decade in Peru, and the Gini coefficient was 49.8 in 2000.[228] Gini coefficient measures how much general incomes deviate from the average[229] which means that the higher the figure, higher the inequality of incomes.

The Bank's impact on the problems of indigenous people and gender issues has been "more indirect that direct, largely through its contribution to economic growth and poverty reduction."[230] When economy did not grow and poverty increased towards the end of the century, the impact on indigenous people and gender issues was not very significant. Also at the beginning of the 1990s the Bank had more pressing issues to deal with than gender equality.

"Peru ranks below the Latin American and Caribbean average on the UN's Gender Development Indicator. The need to focus on economic and political stabilization during the early 90s detracted attention from gender issues. More direct attention was given starting in 1996… The Bank has addressed gender issues both directly (maternal mortality, women's access to markets, property rights) and indirectly through its

[223] Honkkila (1997), 15
[224] FONCODES Staff Appraisal Report 1996, 1.2
[225] The State of the World's Children 1993, 68
[226] The State of the World's Children 2005, 75
[227] Lipset & Lakin (2004), 343
[228] World Development Report 2005, (2004)
[229] Sutcliffe (2002), 7
[230] Peru Country Assistance Evaluation 2002, 22

assistance in health, education and nutrition. Gender indicators have continued to improve."[231]

According to the World Bank, during the 1990s there have been improvements in the lives of women, particularly in health. For example fertility rates have dropped and maternal mortality fallen, but both are still worse than average in countries with equal gross domestic incomes. Illiteracy rate of women (17 percent) is considerably higher than that of men (6.1 percent), and higher than the Latin American average for women (13 percent). Poor women are more likely to be illiterate as the non-poor women are, and nearly half of poor rural women are illiterate. However, for school-age children there is little difference between attendance at schools, which indicates that in the future the illiteracy rate of women is likely to fall.[232]

Critics of the Bank argue that although discourses and practices of development are rarely explicitly marked in terms of gender and sexuality, they are inherently gendered and sexed. For example in the visual representation of women in World Bank literature women are marked as mothers, wives and heterosexual. In addition, women are represented as being poor, illiterate, lacking formal education, traditional and non-white. One way of doing this victimisation of women is through the usage of standard social and economic indicators, ones that are widely used by the Bank. For example through presumably objective indicators such as life expectancy, literacy, sex ration, birth rates, nutrition and income-generating activities, women are determined to be in need and poor and 'underdeveloped'. Or conversely, few of them, well-off and 'developed'. [233]

Women and gender equality have been increasing concern of the World Bank. Kum-Kum Bhavnani argues that although there has been a shift in development studies towards such issues as environment and gender, the policies of international aid agencies, such as World Bank, are still dominated by structural and economistic approaches. The Bank's view on women and their roles is especially economistic. For example the 1992 World Bank Report argued that women must not be regarded as mere

[231] Peru Country Assistance Evaluation 2002, 23
[232] PERU CAS 2002-2006, 4
[233] Lind & Share (2003), 63-64

recipients of public support but as economic agents. The Bank saw women's participation in economic development as a fundamental part of its neoliberal strategy for improving economic productivity. In Bhavnani's view the Bank values poor women as workers and entrepreneurs and ignores women's other roles as wives, partners, mothers, citizens and activists, roles that form the backbone of all societies. These roles are problematic for the Bank, as they are difficult to discern and understand in conventional economic analyses. This is, according to Bhavnani, one reason why the Bank has not been able to engage with the actual realities of people's lives. [234]

Anna Tsing asks in her article, what does the promotion of private corporations and private families and subsequent undermining of public alternatives mean to women and gender equality. She feels that privatisation shifts the possibilities for mobilising women as women. She argues that there is "an equation: democracy equals globalization equals privatization". There are connections between the private sphere of women's feminine containment and privatisation of public goods and spaces, and privatisation is never just an economic strategy, it is suffused with political culture.
"In the United States, privatisation developed in the 1970s and 1980s as part of a neoconservative social agenda, which recognises only two kinds of legitimate social bodies: private corporations and private families. It has called for the destruction of other public goods, practices and institutions, from welfare to public education, environmental regulation, equal opportunity hiring and social services." [235]

In the neoconservative view, governmental spending is fine as long as it promotes families, corporations and their economic or security interests. In Tsing's view, this kind of cultural politics is problematic, because it promotes only individual benefits. Inside it, it is difficult to cross boundaries of class, ethnicity and even marital status to identify with others.[236]

Although the economic growth and better access to infrastructure services has helped the lives of many women, it can be argued that the emphasis of private services increases the workload of women. As private health care and other services are too

[234] Bhavnani, Foran & Kurian (2003), 3
[235] Tsing, Anna (2003), 35-39
[236] Tsing, Anna (2003), 35-39

costly for many households, women are usually those who will need to take care of the children, elderly and those who have fallen ill.
Status of indigenous people has attracted more attention from the Bank since the mid-1990s. When indigenous people are defined as those who speak an indigenous language as their mother tongue, indigenous people are estimated to account for 15 percent of the population of Peru. Their poverty level is 70 percent, which is much higher than the national average. Indigenous families often lack the most basic services, such as running water and sewage. Only 21.4 percent of indigenous households had access to public sewage facilities in the turn of the decade, compared to 71.6 percent of non-indigenous. Non-indigenous men also earn more than two times the wage of indigenous men. [237] The

The Bank conducted a study of Indigenous Peoples, Poverty and Human Development in Latin America, including Peru in 1994 – 2000. As many countries were research, the Bank has used it's own poverty measures instead of the national figures, which explains the difference between these numbers and those used above. According to this study, poverty among indigenous households increased slightly between 1994 and 2000, from 62,3 percent to 62,8 percent, while poverty among non-indigenous households increased from 40.1 percent to 43 percent. Extreme poverty in indigenous households, on the other hand, decreased from 28,6 percent to 22,2 percent and in non-indigenous households, from 10.9 to 9.5 percent in the same period. But still out of every extremely poor households, 52 percent are indigenous. Poverty levels between indigenous and non-indigenous households decreased slightly, but the Bank argues that an increase in the poverty rate of non-indigenous households, rather than a decrease in poverty among indigenous households largely explain this. [238]

Public utilities serve the common interest of society and provide basic services, which are essential to the every citizen. Public utilities, such as water, energy, mass transport and telecommunications have often been in the responsibility of the governments. Public savings, free markets and removal of price distortions are the main goals of the privatisation of public utilities. However, in some cases the efficiency has not improved and prices have gone up and wages down. Many people have had difficulties in paying

[237] PERU CAS 2002-2006. 3
[238] web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/LACEXT/0,,contentM

for their public utilities after privatisation. [239] Prices have gone up also in Peru, which affects all consumers, but especially the poor. Prices have gone up especially in telephone-, electricity- and oil-companies. Privatisation is often justified with the necessity to brake down the monopolies, but new private monopolies have emerged through the process. For example the public telephone companies *Entel* and *Compañia Nacional de Telefonos* were sold in 1994 to *Telefonica*, a company whose largest owner is the ex-colonial power Spain. *Telefonica* got a guarantee from the government of Peru, that it would have a monopoly in Peru for a five-year period. [240]

Also Birdsall and Nellis argue that increases in access to services is often accompanied by increases in prices. The amount and structure of these price increases is such that it produces, in the short-run, increased inequity. This has been the case in Peru as well.[241] After the privatisation the quantity and quality of telephone services did grow significantly but at the same time, the tariffs did also reach a high level. According to Teivainen, similar trends can be observed in many other privatised public services.[242] Often the price increases fall more heavily on the poor, because they spend a higher percentage of their income on the privatised services. Private owners are also keener on collecting arrears and ending illegal water or electricity connections, which are numerous in Latin America. This also effects the poor, as they are more likely the ones who have the illegal connections in the first place. [243] Often wages in private companies are better than in the public ones, but situation can be reversed as well. In Peru, workers in the public water companies are paid almost three times more to do the same work as those who work for the private water contractors[244].

When privatisation increases the ownership of foreigners in a country, it can be seen as a positive from a distributional view, because the sale of shares to foreigners does not contribute to the formation of the country's internal social structure. The sale for foreigners can be seen as preventing the wealthiest of a society from getting richer.[245]

[239] Structural Adjustment, The SAPRI Report (2004), 117-118
[240] Teivainen (1999), 80-81
[241] Birdsall & Nellis (2002),22
[242] Teivainen, (2000), 10
[243] Birdsall & Nellis (2002), 16
[244] Alexander (2004), www.servicesforall.org/htme/worldbank/Peruvians_at_risk.shtml
[245] Birdsall & Nellis (2002),11 and Honkkila (1997), 21

However, the increased ownership of foreigners may cause a sense of unfairness in the society as a whole.[246]

Birdsall and Menezes conclude that analyses of structural reforms, privatisation among them, suggest that Latin America would overall be worse off without them, as per capita income and output would have been lower, volatility higher and poverty deeper. But on the other hand, they feel that the visible benefits of the structural reforms have been small in terms of growth and largely concentrated among those with higher education and initially higher assets.[247]

One way to examine the impact of privatisation on the welfare of people is by examining the popularity of privatisation. Latinbaramoter survey found that in 2001, 63 percent of the people surveyed in 17 countries felt that privatisation had not been beneficial. The figure has risen, as in 1998 45 percent felt this way. Opinion poll in Peru in 2002 found that 21 percent of those interviewed were in favour of privatisation in general. However, 69 percent said that they would be in favour of privatisation if the privatised company invested to expand services, and 65 percent felt that prices could be increased if a regulatory body approved it. 59 percent said that privatisation is acceptable when done in transparent way. [248] Public approval of the privatisation process has decreased steadily in Peru. In 1991, over 50 % of the population approved privatisation, but the approval had decreased to little over 20% in 1999. [249] There has also been much public protest against privatisation. For example in 2002 there was a nationwide strike against privatisation.[250]

After the economic recession started in 1998, largely as a result of external shocks, there have been strong social and political pressures throughout the country. These include demands to reinstate or compensate workers fired from public companies and halt further privatisation and concession of infrastructure and public services. World

[246] Birdsall & Nellis (2002),11
[247] Birdsall & Menezes (2005), 4
[248] Harris (2003), 12-13
[249] Torero (2003)
[250] www.worldpress.org/article_model.cfm?article_id=765&dont=yes

Bank predicted in 2002 CAS that the pace of privatisation will be slowed down in the beginning of the 21st century.[251]

The poverty in Peru after the privatisation process has not been reduced. Many privatised services have extended their services to new areas, but according to other inequality indicators, equality has not increased during the 1990s. One way of reducing poverty and inequality is through effective social security. Next I will focus on privatisation of social security in Peru and its effects on poverty.

The social reforms recommended by the Bank in structural adjustment emphasise the importance of participation of private sector and third sector organisations. Governmental benefits and subsidies have been reduced, and directed only to the poor. The role of the state has been limited to basic services and user charges have been introduced to education and health care. [252] However, according to Veli-Matti Ritakallio, the most ineffective model of social security in reducing poverty is the one promoted by the World Bank, where social services are directed only towards the poor.[253]

In the health sector, the Bank recommends that public sector should fund for example prevention of infectious diseases and pollution, and other factors important to public health. Other than basic health services should be left to the private sector and competition should be encouraged both between private sector actors and between private and public sector. The Bank emphasises that the poor should be guaranteed basic health services. The new policy, which the Bank has recommended since the late 1990s, is that the state should be seen as director, not as a producer of services. [254]

Koivusalo and Tapanainen argue that social and democratic rights of citizens are compromised if they are seen only as consumers by the private health care companies, and as objects of aid by the grass root organisations. They say that the health sector reforms have often lead to a situation were the responsibilities of heath services have been shifted to third sector organisations and women.[255]

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[251] PERU CAS 2002-2006
[252] Koivusalo & Tapanainen (1999), 14
[253] Ritakallio (2000), 39
[254] Koivusalo & Tapanainen (1999), 17, 21
[255] Koivusalo & Tapanainen (1999), 21

The private pension system of Peru was started in 1992. The private pension system was created at the end of the year and the system of pension fund institutions was inaugurated in mid-1993. At the time of these reforms, the Constitution of 1979 was still formally valid and it stipulated that pension and health coverage should be handled by public institutions. This means that the private pension system was unconstitutional at the time. The new constitution, which was accepted at the end of 1993, permitted both private and public pension systems. Teivainen argues that the creation of private pension system was an important step in making neoliberal reforms as irreversible as possible. When people put their savings in private institutions instead of the public social security system, they become investors themselves and their support for policies, which are deemed good for investors increases. Teivainen argues that the growth of private pension funds is likely to increase people's support for investor-friendly policies. Many incentives were given in early 1990s in Peru to encourage people to move from the public system to a private pension system. At the same time, return to the public system was made very difficult. Between 1993 and 1999, over two million people had joined the private pension system, while one million people remained in the public system. [256] As the population of Peru was around 25 million in the late 1990s, the majority of the people were not members of neither of the pension systems.

In some countries, like Chile and Mexico, the government guarantees a minimum pension for workers who do not qualify for it under the private pension system. [257] Peru doesn't have a minimum pension guarantee. According to Carlos Boloña, the minister of finance in Peru at the time when the private pension system was created, minimum pension guarantee presents a moral hazard problem. He believes that it would encourage people to invest their money haphazardly in a hope for huge returns in risky investments. [258] In Peru, workers in the privatised pension system are expected to pay 11.2 percent of their gross wage. [259]

According to Teivainen, the government used several ways in making the reforms irreversible, and one of them was the citizen's participation (*participación ciudadana*)

[256] Teivainen (2000), 11-13
[257] www.larouchepub.com/other/2005/site_packages/ss_privatization/050115memo_
[258] www.pensionreforms.org/articles/carlos_bologna.html
[259] www.larouchepub.com/other/2005/site_packages/ss_privatization/050115memo_

scheme. It started in 1994 and the idea was to extend share-ownership in the privatised enterprises to general public, so that more people would feel that they had a stake in the privatisation process. Teivainen argues that the name of the scheme illustrated "profound changes in neoliberal Peru". With the increasing "privatisation of the public sphere, citizenship was becoming more and more connected to one's purchasing power. Social policies were previously conceived, though not necessarily always practised, as universal measures corresponding to rights that all citizens are legally entitled to. With the neoliberal reforms, social policies became increasingly aimed at specific vulnerable sectors and uncoupled from citizenship." [260]

[260] Teivainen (2000), 13

5. CONCLUSIONS

According to the World Bank, privatisation will increase the welfare of society by decreasing poverty, inequality and corruption and increasing employment. However, although economic development was achieved, poverty and inequality have not been reduced significantly in the 1990s in Peru. Corruption and employment are more difficult to estimate. Both have been big problems in Peru for decades, but the impact of privatisation on either is hard to determine. Direct employment did fell after privatisation, but it has been argued that indirect employment increased more because of economic growth.

There are many ways to determine whether Peru has developed in the 1990s and what role has the structural adjustment and especially privatisation played in the process. The most often used indicator of development is the economic development, which according to the World Bank is essential in increasing incomes, improving social indicators and reducing poverty. The economic growth of Peru has been good, although slightly slower towards the end of the decade. If one estimates the social indicators, such as life expectancy at birth, infant mortality rate and illiteracy rate, Peru has definitely developed in the 1990s. Practically all the social indicators, which the World Bank uses, have improved, although many of them are still lower than the Latin American average. But has this social development been an effect of the Bank advocated policies and privatisation? The Bank itself has acknowledged that many social indicators have improved also in countries, which have not followed the structural adjustment policies. There are certainly many social policies, which can improve these indicators.

There is also evidence that economic growth, on the other hand, is not necessary in improving the social indicators, and on the other hand, necessarily does not improve social indicators. One of the most often used examples is the Indian state of Kerala, where the social indicators such as infant mortality, life expectancy at birth, and literacy rate, are far better than Indian average although the income level of people in Kerala is much lower than Indian average [261]. It is also possible that after country has experienced

[261] for example, Sen (1999), 46

economic growth, this growth does not led to any significant improvements in social indicators. The important questions after economic growth are; whose incomes increased and how are the increased incomes used?

The most important social indicator to which the Bank aims its efforts is poverty. The most important mission of the Bank worldwide and in Peru is the reduction of poverty. This, however, has not been achieved in Peru in the 1990s. World Bank admits that although there has been improvements in living standards in Peru according to many social indicators, poverty has increased since 1997 and this rise “more than wiped out the gains made between 1994 and 1997 when poverty fell”. [262] According to World Bank, every time when GDP rises, also the income of the poor rises, and when the GDP drops, also the income of the poor would be lower.[263] This would naturally mean that when the GDP rises poverty is decreased, because many poor would have enough income to rise them out of poverty. Or at least over the poverty line. The Bank argues that the rise and fall of poverty rates are ‘mirroring’ the rises and falls of per capita GDP. The fact that poverty did decrease in the mid-1990s when the growth of GDP was fastest does support this presumption.

However, the poverty rate in Peru was roughly the same at the beginning of the decade than it was in 2000, although the per capita GDP had nearly doubled. This shows that at least in Peru, economic growth was not enough to reduce poverty. Another problem is that although the income of the poor would increase when the GDP grows, the poor might still be worse off, because they need to spend more money on their everyday life than before. Privatisation has increased prices and the poor need to spend more to be able to use privatised services.

One interesting feature of the Bank’s speech of poverty is that the reasons of poverty are very rarely discussed. The ’dimensions of poverty’, which mean the various ways in which poverty affects peoples lives, are discussed, as well as the question of ’rising from poverty’; what people need to do to ’brake the vicious circle of poverty’. But the social, political and economic reasons for existing poverty, the question what makes some people poor, were not mentioned in the texts I have read. Marketta Lindberg has

[262] PERU CAS 2002-2006, 2
[263] Tammilehto (2003), 21

studied the language the Bank uses and has find that the Bank tends to personify ’poverty’ and this way make it a concrete, recognisable enemy. This way Poverty is more easily defeated than some abstract condition in which people in developing countries live in. In addition, Poverty is created as a concrete enemy, a subject, and the Bank can avoid naming those people whose actions could have created poverty. [264]

The fact that economic growth has not reduced poverty brings up the question of distribution of the benefits of growth. There was economic growth in Peru in the 1990s, but who did benefit from it? Who got the increased incomes? In theory there should have been a more straightforward impact of economic growth on poverty. One explanation of this is that the growth benefited those who already were above the poverty line, not those living in poverty. This leads to more thorough examination of the concept of equality. In many countries since 1980 national income has gone up, but so has inequality, which means that poverty has not been reduced [265].

Equality is often seen as one aspect of development. Developed society is an equal one. The World Bank defines equality as an equal access to basic services, such as education, health care and infrastructure, and equal opportunities to pursue better living standards. In the latest World Development Report 2005, the Bank sees the question of equality concerning mainly the prerequisites for development, not the equal distribution of the outcomes of development. This, from my point of view, seems to be an inadequate definition of equality. Equality is not just the access to basic services, but to the basics of living, such as nutrition, clean water, housing and security. Equality means respect of human rights of all. Equality helps to maintain social peace and creates trust, which reduces corruption. Equality supports democracy and generates economic growth. Very often the question of equality in the context of development is the question of gender and ethnicity.

One reason for existing poverty is inequality, that few in a society have most of the wealth, and majority are have very little power, rights, education, land, and money. What is needed for reducing poverty is more equal society, more equal distribution of benefits of growth. Equality of income distribution does not mean that everyone should

[264] Lindberg (2004), 99
[265] Tammilehto (2003), 23

have the same amount, or even that everyone should have income according to their workload, as there are many, such as the elderly, the sick and the unemployed, who should have their share of the cake even though their input is limited. Privatisation has increased inequality in Peru, which is one reason why poverty has not decreased. If the economic benefits of privatisation are considered to be significant, then government should pay more attention on how these economic benefits are divided among citizens. The World Bank argues that one benefit of privatisation is that governments can use revenues from the sale of public enterprises in human capital development. However, often there have been more pressing expenditures for these revenues, such as paying off foreign debt.

According to the many World Bank standards, development in Peru in the 1990s has been fairly good. Privatisation has brought services to new, often poor customers and these people have better opportunities in bettering their lives. Economy has grown, which is believed to be beneficial to the whole country. It is believed that privatisation decreased unemployment and underemployment in the long run, although this is hard to prove, as the employment figures in Peru are very unreliable. It is also difficult to determine the effect of privatisation on corruption. The essence of corruption is such, that it is almost impossible to have any reliable statistics of its changes. Many health and other social indicators show signs of approving in Peru after privatisation, although the trend was positive also in the 1980s, during a very different economic policies. But if one would determine development solely on the basis of the Bank's most important development indicator, poverty, then is could be argued that the theory of privatisation and development has not worked in Peru.

The World Bank's concept of development has blended in so many different aspects, that almost any action is bound to achieve at least one of them. It cannot be said that privatisation in Peru had failed, as it has resulted in many good consequences. But the Bank's economistic view of development has created much criticism and different views of development have been created.
Questions of economic growth, poverty and income equality are all economic questions, although they naturally have great impact on human, political and social development. Nevertheless, as important as they are, it does not give a whole picture on development. According to Prabhu, in the context of formerly colonialist countries, development is

tied to the idea of (new) nation, with the nationalist rhetoric of development being clearly linked to catching up with the 'mother' country and to modernisation. The WCD paradigm calls for a retreat from these simplistic definitions of development, where the development is identified with modernisation and measurable economic progress.[266]

In the Women, Culture and Development (WCD) point of view, development is social, economic, political and cultural change, which does not privilege the economic above other domains and sees the culture as lived experience. Political economy is not seen above culture, but the two are seen as operating simultaneously and in synchrony. Development can be defined as well-being and creativity in all domains of life. [267] The WCD approach challenges the idea that development looks the same in every part of the world, and suggests that progress should be defined locally. The emphasis on agency and culture provides better tools to understand what people think and care about, and also a way to analyse the differences of power within communities, such as those based on hierarchies of wealth, sex/gender and race. WCD approach also proposes a critique of development that is not founded in 'Third World victim status', which means that development is not seen as something that is 'done to' the Third World, but there is an acknowledgement that Third World actors, men and female, contribute to the construction of the discourse and practice of development. WCD challenges conventional understandings of development, "because it permits a careful analysis of local level processes without losing sight of their constitutive role in relationships between nations and economies and vice versa".[268] The main argument for the WCD paradigm is the urgency to move away from economistic analyses, in order to understand people's lives and agency in all their complexity. [269]

From this approach, the measures which the Bank offers in order to assess the impact of privatisation on development are inadequate. In its own growth standards development in Peru has been good in the 1990s and the Bank has praised the speed with which the privatisation process was conducted. But what it comes to poverty rates, development has failed as the growth and better access to privatised services has not reduced poverty. But as the Bank has said, development is about human lives, happiness, about people's

[266] Prabhu (2003), 240
[267] Bhavnani, Foran & Kurian (2003), 10, 15
[268] Carruyo (2003), 200-201
[269] Prabhu (2003), 239

rights and possibilities of acting as they feel right for themselves and their society. Privatisation has been widely criticised and opposed in Peru, and when the government did halt some privatisation negotiations at the end of the 1990s, the Bank criticised it for doing so. The Bank often argues that governments should not back out of projects because of public resistance. The Bank feels that these decisions are made only to get votes in the next elections, and does not see that as people strongly oppose to something, it might have actual difference in their lives, perhaps even more important than economic growth.

Privatisation often means that people who cannot afford these services any more, or live in an area where the services have not reached, don't have any way of urging these privatised services. If services would be offered by the state, people would have some power as voters in trying to fight their rights as citizens. When a service is private, people only have power as consumers, which means that those who have more money have more power. This increases the inequality and creates sense of unfairness in a society. There is a missing link in the Bank's argument that economic development reduces poverty, and that is inequality. Many aspects of privatisation increase inequality and government, both local and central, should try to balance the situation so that poverty could be reduced.

The difficulty of assessing the benefits of the Bank advocated development policies raises the question; how well justified is the Bank's power in development field. The World Bank still values economic indicators higher than any other indicators, when assessing development. It all comes down to economic efficiency and growth. More complex definitions of development can and have been given, but as it is difficult or even impossible to measure them, there is no way of impeccably determining whether something, in this case privatisation, has been beneficial for development or not. These difficulties have led some theorists to dream of a post-development era or end of development. Development has to some people lost its meaning as something good and desirable, and has become a colonial word, something that justifies poverty and inequality.

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