Privatization, Distortions, and Productivity *

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Abstract

I develop a new framework for analyzing the direct and indirect effects of privatization on productivity and distortion. To do so, I propose a novel method to jointly estimate distortions, productivity and production function parameters. I then apply the method to Chinese National Bureau of Statistics (NBS) industrial annual surveys from 1998 to 2007. I find that when a firm is privatized, it immediately realizes a 5% increase in productivity, which is equivalent to one year of productivity growth for an average manufacturing firm in the sample. Coupled with the estimated persistent productivity process, overall privatization increases privatized firms’ productivity about 14% at 2007. Meanwhile, privatization reduces distortions by 2%. Privatization directly contributes 5% in the aggregate productivity growth in the sample, mainly through its impact on firm productivity. In contrast, the gains from improved factor reallocation due to privatization appear to have limited effects on firm revenues and aggregate TFP.

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