WJEC (Wales) Economics A-level
Microeconomics

Topic 2: Market Structures

2.8 Privatisation

Notes

Nationalisation:

- This occurs when private sector assets are sold to the public sector. In other words, the government gains control of an industry, so it is no longer in the hands of private firms.
- The railway industry in the UK was nationalised after 1945.
- By nationalising an industry, natural monopolies are created. This is because it is inefficient to have multiple sets of water pipes, for example. Therefore, only one firm provides water.
- Some nationalised industries yield strong positive externalities. For example, by using public transport, congestion and pollution are reduced.
- Nationalised industries have different objectives to privatised industries, which are mainly profit driven. Social welfare might be a priority of a nationalised industry.

Deregulation and privatisation

By deregulating or privatising the public sector, firms can compete in a competitive market, which should also help improve economic efficiency.

Deregulation is the act of reducing how much an industry is regulated. It reduces government power and enhances competition.

Excessive regulation is also called 'red tape'. It can limit the quantity of output that a firm produces. For example, environmental laws and taxes might result in firms only being able to produce a certain quantity before exceeding a pollution permit. Excessive taxes, such as a high rate of corporation tax, might discourage firms earning above a certain level of profit, since they do not keep as much of it. This might limit the size that a firm chooses, or is able to, grow to.

Privatisation means that assets are transferred from the public sector to the private sector. In other words, the government sells a firm so that it is no longer in their control. The firm is left to the free market and private individuals.
For example, British Airways was privatised in the UK and now operates in the competitive market.

Free market economists will argue that the private sector gives firms incentives to operate efficiently, which increases economic welfare. This is because firms operating on the free market have a profit incentive, which firms which are nationalised do not.

Since they are operating on the free market, firms also have to produces the goods and services consumers want. This increases allocative efficiency and might mean goods and services are of a higher quality. Competition might also result in lower prices. However, firms which profit maximise in a competitive market might compromise on quality.

By selling the asset to the private sector, revenue is raised for the government. However, this is only a one-off payment.

The Royal Mail was privatised in the UK. This was done by allowing the Royal Mail to float on the stock market. At the offer price, the government owned 30% of the shares.

The arguments for and against the public ownership of firms and industries

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The arguments for and against the privatisation of state-owned enterprises

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- It also covers the deregulation of the market.
- For example, British Airways was privatised in the UK and now operates in the competitive market.
- Free market economists will argue that the private sector gives firms incentives to operate efficiently, which increases economic welfare. This is because firms operating on the free market have a profit incentive, which firms which are nationalised do not.

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- Competition might also result in lower prices.
- By selling the asset, revenue is raised for the government. However, this is only a one-off payment.