ENTERPRISE-STATE RELATIONS AFTER MASS PRIVATIZATION: THEIR CHARACTER IN MONGOLIA

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1. Introduction

A changing relationship between state and enterprise is one central element in the economic reforms of post-socialist countries. In most reforming countries, mass privatization has been a prime ingredient in a menu of policies designed to sever the old links between state and enterprise and to channel interactions into the legal and regulatory form characteristic of developed, capitalist democracies. Thus, an important indicator of progress in the microeconomics of transition is the condition of enterprise-state relations after mass privatization. In this paper, we present a comprehensive description of those relations in one formerly Soviet-bloc country, Mongolia, which adopted a comprehensive, voucher-privatization scheme early in its reform program.

We focus on description, pulling together fragmentary information on the varied aspects of enterprise-state interaction. The purpose is to provide an overall picture, rather than examining causal underpinnings. Nevertheless, in providing description, we are able to subject to scrutiny common assumptions about the nature of enterprise-state relations in transition countries.

Not surprisingly, we find evidence of a state that interacts with enterprises in multifarious ways, many of which are hardly consonant with the role of the removed regulator that is the presumed objective of mass privatization. The image of the state as an absentee owner, which was popular in the early analysis of transition, does not coincide with the evidence presented here. We find that intensity of interaction is strongly related to the degree of residual state ownership in enterprises: enterprise-state interactions tend to be concentrated in a subset of enterprises. Indeed, our results suggest the incipient creation of two different privatized sectors, one in which there is residual state ownership, which accounts for a large proportion of enterprise-state interactions, and one in which there has been complete privatization, more removed from the state.

Our results come from one country, Mongolia, and therefore we can make no claims to generality. Rather, the purpose is simply to add one data point to the stock of information on transition processes. This is especially the case for the poorer, more isolated countries for whom reforms involved a much more severe logistical and administrative problem, since there is still a dearth of post-privatization evidence on countries outside Central and Eastern Europe and Russia.

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Among such countries, Mongolia's *de facto* political status as the 'sixteenth republic' ensured that it had the economic conditions, the ensemble of institutions, and the industrial structure of a poorer ex-Soviet republic. But its *de jure* independence meant that it began reforms earlier then comparable countries. Mongolia also pursued privatization more vigorously than did most other reforming countries. Its privatization scheme was relatively successful in channeling a large number of enterprises through a consistent process in a short time. Section II of this paper presents the background information on Mongolia's privatization process that is necessary to place in context the evidence of later sections.

As has been frequently noted, privatization invariably results in the state retaining ownership in a significant proportion of enterprises.[1] Mongolia was no different, as we document in Section III, presenting information on the size and distribution of retained state ownership. Section IV examines the state's formal involvement in the enterprise by focusing on the composition of corporate governance bodies and the presence of government officials on these bodies. That section also analyzes data on whether enterprises perceive the supervision of a particular state entity, providing evidence that the state is not an absentee owner.[2]

Section V looks at how enterprises lobby when pursuing their political goals. We find clear evidence that the lobbying activities of completely private enterprises differ from those of the enterprises with residual state ownership. The latter rely more on traditional ties, while the former tend to make more use of newer channels that have been made possible by the establishment of democracy.

In section VI, we turn to subsidies and soft budgets. We examine a variety subsidies, such as those through the banking sector and through tax authorities, as well as direct state funding of enterprise activities. Again, there is a clear relation between the degree of subsidization and the extent of state ownership. This relationship is stronger for more explicit forms of subsidies, and quite often non-existent for less explicit ones, such as tax arrears and commercial bank funds. This latter observation suggests that aid to state enterprises is part of the open political process, rather than being hidden in the arcana of governmental decisions. Section VI examines whether the subsidization translates into managerial perceptions of soft budgets, suggesting that managers in the state sector might be somewhat more optimistic about state aid in troubled times than the objective evidence on subsidies would justify.

Sections VII and VIII turn to the state's involvement in transactional process. In an institution-poor transition environment, a state wishing to pursue the public welfare could certainly find market failures in need of correction. The beneficent state could find opportunity to act as facilitator of transactions and resolver of disputes, while a venal administration could intervene in a manner that is common in the characterizations of the rent-seeking literature. While our data do not allow us to determine which type of state we are observing, they do show a high level of state activity in enterprise transactions. As customer, the state is involved in a significant proportion of enterprise sales, some of which enterprises view as mandatory purchases. The state also plays a large role as mediator of disputes.

Section IX concludes by looking at the degree of concentration of enterprise-state interactions. Clearly, a narrow set of enterprises is the most frequent object of the state's attentions, and these enterprises are ones with a high share of residual state ownership. The picture that emerges is of a cohesive state sector that has arisen after the privatization process.

2. Mongolian Privatization[3]

After a peaceful revolution and democratic elections in Mongolia in 1990, a broad coalition government began sweeping economic reforms. The centerpiece of these reforms was privatization, which occurred in three different programs, for small enterprises, large enterprises, and agriculture. Here, we focus on the privatization of the large enterprises, which began in March 1992. In the next four years, 483 large enterprises were privatized: 55% in 1992, 30% in1993, 12% in 1994, and 3% in 1995.

On the supply side, large privatization was highly centralized, with enterprise themselves having little scope for decision-making. All large enterprises went through the same method of privatization. The state retained ownership interests in some enterprises, decisions on the size of which were made by a tangle of actors. In the early critical phases, the Privatization Commission, which had the power to make detailed decisions, was led by a politician advocating the most extensive reforms possible and was staffed by like-minded individuals. The Privatization Commission was an arm of a government that was much more conservative, but which tended to ignore the details of privatization. Guidelines, which defined the enterprises that were to remain under some degree of state ownership, could be loosely interpreted by the Privatization Commission staff. Enterprise insiders, who had no formal power whatever, could nevertheless use obfuscation and delay to push their interests. Informal bargaining rather than open debate led to the decisions on residual state shares.

Once the state share was decided in the context of the approval of a privatization plan, an enterprise was corporatized. At that time, control shifted into the hands of the general director, the workers, and the Privatization Commission, as putative representative of future shareholders. Enterprise shares were then scheduled for sale on the stock exchange, not for cash but for vouchers.[4] Every citizen had received a set of seven non-tradeable vouchers for large privatization. Markets, in which vouchers were exchanged for shares, determined the allocation of enterprise shares between individuals. Enterprise employees could buy shares in their own companies and this was a very popular option. In the sample of enterprises that forms the basis for this study, the mean residual state share is 20%, insiders and their families own 35%, and outsiders 45%.

In Mongolia, as in many other transition countries, insider owners can more easily gain representation on corporate bodies than can non-state outsiders. On the one hand, insider shareholding probably resulted from concerted efforts on the part of employees to hold a large share in their own enterprises (Korsun 1995). On the other, non-state outsiders had few mechanisms to create blocks of shares. Investment funds have not been popular and have a significant ownership share in only a small number of enterprises. Vouchers were non-tradeable, so that initial share ownership was diffuse. The secondary trading of shares officially began only in August 1995, only ten months before our data was collected. Although there was heavy trading of stock in that ten months, this is a limited amount of time for formation of significant outsider power. By mid-1996, only thirteen percent of enterprises reported any presence on their boards of individuals representing investment funds or large outsider shareholders.

Other aspects of reform proceeded continuously throughout 1991-1996, although not without many setbacks on the way.[5] Formal liberalization of the economy was announced very early in the reform process, but actual liberalization proceeded more slowly, due to the effect of lingering interventions. By the end of 1993, after the failure of initial attempts at stabilization, runaway inflation no longer was a danger. However, since that time, successive governments have been in a struggle to maintain fiscal balance, with one consequence being that inflation remained just above 50% in 1995 and 1996. Growth resumed by the middle of 1993, after a relatively mild (for transition countries) fall in GDP of 18%. But concurrent with that fall, there was a catastrophic drop in living standards as a result of the withdrawal of Soviet aid, which during the 1980's had been as high as 30% of Mongolian GDP.

In mid-1996, we surveyed 249 enterprises in Mongolia, well over half of the enterprises that had passed through the large privatization program. The survey covered all enterprises in the national capital, Ulaanbaatar, and all enterprises in the regional centers of eight of the remaining twenty-one administrative districts (aimags) of the country. The response rate for the survey was effectively 100%.

3. Size and Distribution of State Ownership in the Privatized Sector

As has been frequently noted (Pistor and Turkewitz, 1996, Brom and Orenstein 1994, Earle, Frydman, and Rapaczyinski,1993), mass privatization invariably results in the state retaining partial ownership in a large number of enterprises. Mongolian privatization was no different in this respect, as Table 1 shows. State ownership averages 20.1% across the sample of enterprises: 56% of enterprises have no state ownership, 13% have state minority ownership, and 31% have state majority ownership. The spike in the distribution at 51% obviously suggests the aim of retaining a controlling interest in a sizeable proportion of privatized enterprises. The distribution of state ownership shares is roughly similar to that found by Pistor and Turkewitz (1996, p. 197) after the first wave of privatization in the Czech Republic. Russia has less residual state ownership, with estimates for that country in the 10-13% range (Dolgopiatova, 1995 p. 10 and Shleifer and Vasiliev, 1996, p. 72.)

The 20% mean state share might be a poor indicator of economic importance if state ownership were correlated with enterprise size. Table 2 therefore presents some weighted means of the state share, using four measures of enterprise size as weights.[6] Two different enterprise valuations were generated during the privatization process, one based on the book value of net assets and the other reflecting the relative

Table 1 - THE DISTRIBUTION OF RESIDUAL STATE OWNERSHIP IN MONGOLIAN PRIVATIZED ENTERPRISES

Percentage state ownership	Number of Enterprises	Percentage share of the sample of enterprises
0	140	56.2
1 -19	6	2.4
20-29	8	3.2
30-39	11	4.4
40-49	6	2.4
50-59	66	26.5
60-69	6	2.4
70-79	0	0.0
80-89	3	1.2
90-99	3	1.2

valuations that Mongolian citizens placed on the enterprises when vouchers were used to buy enterprise shares. The second and third rows of Table 2 report the size of the state share based on these valuations, indicating that the state retained shares in enterprises that were larger than average.

In 1995, the re-trading of shares began. In preparation, accounting data on the book values of enterprises in 1994 were circulated widely in the media.[7] The value of the state share based on these values is given in the fourth row of Table 2. There is a small decline from the analogous value at the time of privatization. Much more remarkable is the change in investors' valuations of the relative worth of enterprises having a residual state share. Between the initial public offering and the first ten months of re-trading, the value of the state's residual share fell from 29% of the privatized sector to 19%, according to the reckoning of investors.[8] Note, however, that these two stock market valuations represent the assessments of two different sets of investors. During privatization, all Mongolian citizens made investment decisions with their vouchers, each citizen having an equal amount of voucher purchasing power. In subsequent trading, buyers used cash, the primary buyers being insiders aiming to increase their stake in their own enterprises and large outsider-investors hoping to obtain controlling stakes.

One obvious dimension along which one might expect state-owned enterprises to differ from those with no residual state ownership is in sectoral composition.[9] Of seven aggregate sectors, the state tended to retain higher shares in enterprises in the agricultural products sector and in wholesale trade, a large share of the latter being concerned with the procurement and distribution of agricultural raw materials and processed agricultural products. This sectoral composition is consistent with the regional distribution of residual state ownership, which is higher in rural areas.

Table 2 - MEASURES OF THE PROPORTION OF THE PRIVATIZED SECTOR OWNED BY THE STATE

Weight used in calculating mean state share	Weighted mean of the percentage state ownership of privatized enterprises
Unweighted	20.1
Book value of enterprise at time of privatization	31.9
Stock market valuation of enterprise in the voucher denominated auctions	29.4
Book value of enterprise in 1994	29.9
Stock market valuation, using average price in the first ten months of secondary trading	19.2

4. Formal Ties Arising from Ownership

A simple way of ascertaining whether state ownership is meaningful is to ask enterprises know which specific authority exercises the state's ownership rights. In the enterprises with state ownership, fully 91% of respondents identified a specific government entity. Moreover, 65% of enterprise directors met with this authority at least once a month to discuss enterprise affairs, a rather large figure in view of the sometimes formidable costs of such meetings in this poor, but vast, country. Evidently, the state is not a disinterested owner.

The Partnership and Company Law of Mongolia of 1995 gives shareholders the power to select two boards. The 'Board of Representatives' is analogous to a U.S. board of directors. Such boards came into existence significantly after many enterprises were privatized, because the first company law, the Economic Entities Law of 1991, did not mandate their formation.[10] The 'Auditing Board' has deeper and murkier roots in the process of transition. It is the institutional successor of the only board originally mandated for privatized enterprises in the Economic Entities Law, the 'Control Council.' The Control Councils were a curious hybrid between the monitoring units of the old centralized administrative system and a German-type supervisory board, a group of outsiders elected by shareholders to monitor company operations. According to the 1995 Law, the declared functions of the auditing boards are much closer to those of an auditor. But there is still some rather broad language; for example, the auditing boards are to 'supervise the activities of the management of the company.'[11]

Tables 3 and 4 present data on board membership. The central conclusion from Table 3 is that the state's ownership interest is represented. The formal mechanisms

Table 3 - SIZE OF STATE REPRESENTATION ON CORPORATE BOARDS

Set of enterprises	Percentage Membership of the Board of Representatives: Means Over Sets of Enterprises			Percentage Membership of the Board of Auditors: Means Over Sets of Enterprises		
	State officials in official role	State officials in unofficial role	All state officials	State officials in official role	State officials in unofficial role	All state officials
All	13.1	1.7	14.9	28.3	6.4	34.7
No state ownership	1.6	3.1	4.8	16.0	9.1	25.1
Minority state ownership	19.9	0.0	19.9	33.4	3.2	36.6
Majority state ownership	31.0	0.0	31.0	48.3	2.8	51.1

Table 4 - PRESENCE OF STATE REPRESENTATIVES ON CORPORATE BOARDS

Set of enterprises	Percentage of Enterprises with Government Representation on:		
	Board of Representatives	Board of Auditors	One or both of the boards
All	46.4	48.1	63.7
No state ownership	17.0	34.8	41.5
Minority state ownership	64.5	51.6	80.6
Majority state ownership	89.3	69.3	94.7

of corporate governance are working, at least as evidenced by these rudimentary measures, since state representation is aligned with ownership. But the proportion of board membership is not necessarily the correct measure of the strength of the state's representation: an overwhelming army need only send a single messenger. Therefore, Table 4 provides evidence on how many enterprises have some state representation on their boards. That evidence suggests that the state's presence reflects more than just ownership: for example, fully 41% of enterprises with no state ownership have a government official on at least one of the boards.[12]

There is a clear difference between the two boards: governmental membership on the board of representatives is more closely aligned with ownership than it is for the board of auditors. There are two possible reasons explanations. Perhaps, the state still wants a role in monitoring the affairs of privatized companies and is able to use its power to gain a presence on the monitoring board, the board of auditors. Alternatively, the historical generation of the two boards might provide the explanation. The boards of representatives were usually formed significantly after privatization, when private owners were natural candidates; the pre-cursors to the boards of auditors were formed before privatization, at corporatization, before private owners were known. Inertia could then explain the larger government presence on the boards of auditors.

5. Lobbying

Lobbying is the opposite side of the picture from government representation on boards, enterprises reaching out to affect policy. Survey respondents rated the importance of different methods of lobbying, via members of parliament, officials of the parent or former parent ministry, government officials who are acquaintances, management of other enterprises, and business associations. The lobbying route most indicative of the continuation of past ties based on state ownership is the use of officials of a parent or former parent ministry. The route most representative of the new institutions of market democracy is the use of a business association or formal lobby group. The data on the use of these two lobbying options are presented in Table 5.

Not surprisingly, contacts with ministries are more important for enterprises with a residual state share, indicating that ownership provides a formalized role for contact with the old structures. The enterprises with no state ownership tend to use associations more than the enterprises with state ownership. But there is still much overlap between the methods used by the different types of enterprises. One view of the privatization process is that it was a means of breaking the power of ministries,

Table 5 - IMPORTANCE OF TWO DIFFERENT TYPES OF LOBBYING CONTACTS

Set of enterprises	Type of Contact	Importance of Contact (% of enterprises) Very Important	Important	Not important
All	Ministries	13	53	34
	BA/LG	18	51	31
No state ownership	Ministries	9	47	44
	BA/LG	25	53	22
Minority state ownership	Ministries	16	61	23
	BA/LG	6	48	45
Majority state ownership	Ministries	17	62	22
	BA/LG	10	50	40

BA/LG: Business Associations or formal lobby groups and for Russia, Shleifer and Vasiliev (1996, p. 68) claim that this strategy was effective. The data in Table 5 give equivocal evidence on this point for Mongolia. Clearly, the old ministries are less important for completely privatized enterprises. Nevertheless over half of the enterprises with no state ownership list a former parent ministry as an important contact in the lobbying process.

6. Subsidies and Soft Budgets

Privatization aims to harden budget constraints, both in actuality and in perceptions. Our data reflect on both aspects.

Enterprises gave information on whether they had received a variety of subsidies in the previous fiscal year: funds or loans for investment, direct subsidies, credit with interest rates below the market rate, tax relief, or debt relief.[13] Table 6 summarizes this information, listing the percentage of enterprises that had received at least one subsidy. While the reported twenty-two percent is in the context of a government facing severe fiscal constraints, this level of subsidies is significantly below that observed in a similar survey of Russian enterprises (Alfandari, Fan, and Freinkman, 1996 p. 167, 185; Earle, Estrin, and Leshchenko 1996, p. 228.) While the presence of subsidies is correlated with state ownership, nevertheless of the fifty-eight subsidized enterprises, twenty-three have no state ownership.

Table 6 - THE PROPORTION OF ENTERPRISES RECEIVING SUBSIDIES

Set of enterprises	Percentage of enterprises reporting that they received subsidies in 1995
All	22.5
No state ownership	16.4
Minority state ownership	25.8
Majority state ownership	32.1

Basic accounting data give a complementary view of the financial interactions between government and enterprise. Kornai (1993, p. 316) cites financial subsidies, tax concessions or postponing tax commitments, rescheduling of loan payments, and providing new soft loans as the primary ingredients of soft budget constraints. In Poland, for example, tax arrears rather than explicit subsidies are the primary mechanism of soft budgets (Pinto et al 1993, p. 245; Belka et al 1994 p. 11.) As Table 7 shows, tax arrears are a significant source of implicit state aid for Mongolia enterprises, although the fact that more enterprises are in arrears on profits tax than on social insurance suggests that tax arrears are not simply due to less profitable enterprises being unable to pay. In contrast to the analyses presented above, and also in contrast to the situation in Russia and Poland (Belka et al 1994 p. 31; Earle, Estrin, and Leshchenko, 1996, p. 228), there is no evidence that tax arrears especially help state-owned enterprises.

Table 7 - INDICATORS OF ENTERPRISE SUBSIDIES THROUGH THE TAX SYSTEM

Set of Enterprises	Effective corporate income tax rate for those enterprises earning positive profits	Percentage of enterprises earning positive profits that were assessed corporate income tax	Percentage of enterprises with more than one year's worth of corporate income tax liabilities	Percentage of enterprises with more than one year's worth of social insurance liabilities
All	0.28	82.9	22.5	15.9
No state ownership	0.25	77.6	25.0	16.0
Minority state ownership	0.29	83.3	25.0	14.3
Majority state ownership	0.33	90.8	17.6	16.4

Table 8 focuses on loans, which are important to examine since there is deep government involvement in commercial banking, including ownership. It is difficult to make a case that the commercial banking sector is a large source of subsidies. With inflation approximately 3.5% a month, interest rates are at high real levels. The proportion of enterprises overdue on payments is below 10%; much smaller than those in arrears on taxes in Mongolia; much smaller than similar figures for Russia (Fan, Lee, and Schaffer, 1996, p. 149) and less than in the Czech Republic (Rona-Tas, 1996 p. 26).[14] Enterprises with state ownership have slightly lower interest rates than do other enterprises, but have no greater tendency to be overdue in their loan payments, nor to borrow from commercial banks.[15]

Table 8 - THE PREVALENCE OF LOANS, THE LEVELS OF INTEREST RATES, AND THE EXTENT OF OVERDUE PAYMENTS

Set of enterprises	Percentage of enterprises with current loans	Average monthly interest paid on loans from commercial banks	Percentage of enterprises overdue on loans from commercial banks	Percentage of enterprises receiving loans from the state	Current loans from the state as a proportion of total current loans
All	33.9	6.10	9.4	9.5	22.8
No state ownership	37.0	6.29	10.8	5.9	14.9
Minority state ownership	21.4	6.25	3.6	7.1	33.3
Majority state ownership	33.8	5.72	9.3	16.2	33.8

Table 9 - THE PERCENTAGE OF ENTERPRISES UNDERTAKING INVESTMENT AND THE IMPORTANCE OF STATE FUNDING

Set of enterprises	Percentage of enterprises with positive investment during 1995	Of those enterprises currently investing, the percentage that uses state funds for investment	Percentage of investment expenditures derived from state sources
All	41.3	7.6	5.7
No state ownership	37.5	4.4	4.4
Minority state ownership	32.1	0.0	0.0
Majority state ownership	50.7	13.2	8.5

But enterprises also borrow from the state.[16] The last two columns of Table 8 provide pertinent evidence. Majority state-owned enterprises have superior access to state loans.[17] Of course, the main channel of funds to enterprises under the old system was not loans but rather direct aid, especially for investment projects. Table 9 shows that this source of funds has fallen to very low levels; Dolgopiatova (1995 p.15) found state sources of investment four times more frequent in Russia. Nevertheless, state enterprises receive the lion's share of such resources.

To what extent do these financial interactions translate into perceptions of soft budgets? The existence of subsidies, of course, is not the synonymous with soft budgets, because subsidies can be unrelated to enterprise performance (Kornai, 1992a p. 10). Similarly, the absence of explicit subsidies, does not imply hard budget constraints, since assistance can be channeled in ways other than direct financial subsidies. Thus, we asked enterprises the following question designed to elicit their understanding of the likelihood of state aid if their enterprise came upon hard times:

Suppose that unfortunate market conditions resulted in a sudden drop in your enterprise's revenues, so that you might have to lay off workers. How likely is it that the government (either national or local) would help your enterprise out, so that it would not be forced by its financial situation to layoff workers? Please indicate your expectation of the likely government reaction by choosing a point on a scale from 0 to 10 — a '0' means you that think that the government would do absolutely nothing to help out and a '10' means that you think that the government would completely make up for the decline in revenues in some way, and a '5' means the government would make up half the decline in revenues.[18]

According to Table 10, 27% of enterprises expect some form of help when their enterprises are in distress; 13% expect that the government would make up more than half of a decline in revenues. By changing scale, one can interpret the answers to the above question in terms of the 'degree of softness' of budget constraints. For example

Table 10 - PERCEPTIONS OF SOFT BUDGET CONSTRAINTS

Set of enterprises	Percentage of enterprises choosing score on the soft budget scale					Means of the enterprise responses
	0	1-4	5	6-8	9-10	
All	73	12	6	4	3	1.23
No state ownership	81	13	1	2	3	0.75
Minority state ownership	77	12	6	3	0	0.78
Majority state ownership	58	13	13	11	6	2.41

(see last column of Table 10), the mean score is 1.23, which indicates that on average enterprises believe that 12.3% of lost revenues will be made up by government. There is significant variation across ownership types: for non-state enterprises it is 7.5% of revenues and for state-majority owned 24.1% of revenues.[19]

One question that naturally arises is whether the perceptions of enterprises seem justified given the previous figures on financial interactions. For example, comparing Table 6 to Table 10, 22.5% of enterprises reported some kind of subsidies, while 27% reported an expectation of a soft budget. For majority state-owned enterprises, 32% received subsidies while 42% expect soft budget constraints.[20] This suggests the possibility of over-optimism concerning state aid, especially for state-owned enterprises, possibly reflecting lags in expectations as described by Kornai (1993, p. 332): '...when financial discipline is being applied more forcefully, [a] quite long period must pass before the actors in the economy start believing that the state's conduct in this respect has changed for good and all.'

7. The State as Customer

The state is a customer with an equivocal character. When buying, the state could be using its power to pursue goals other than economic efficiency, perhaps using mandatory purchases as a politically cheap means of taxation. Nevertheless, in an environment where market infrastructure is extremely poor, and where only a few years ago the state was the sole provider of distribution services, it is possible in principle that state purchases represent efforts to fill market lacunae. Additionally, of course, there are state purchases normal in any country, needed for the provision of public goods.

Because of this ambiguity in the role of the state as a customer, the survey aimed to discern which state purchases were on a commercial basis and which involved compulsion. Enterprises were asked which sales to the government were freely

Table 11 - SALES TO THE GOVERNMENT AS PERCENTAGES OF TOTAL SALES

Set of enterprises	Sales with government involvement (as buyer or intermediary) as a percentage of all sales	Sales mandated by the government as a percentage of all sales
All	18.4	7.1
No state ownership	14.1	5.0
Minority state ownership	22.7	8.6
Majority state ownership	24.4	10.3

negotiated and which ones were mandated.[21] The data in Table 11 show that 18% of sales go to the government on average, a dramatic change from five years previously when over 60% of enterprise sales were mandatory state orders. This is a higher percentage than observed by Belka et al (1994 p. 16) in Poland in 1992 but significantly lower than in Russia (Alfandari, Fan, and Freinkman 1996, pp.167, 186; Earle, Estrin, and Leshchenko, 1996, p. 228.) As in Poland and Russia, the proportion of sales that go to the state is correlated with state ownership.

Still, enterprises classify more than one-third of sales to the state as mandatory, a low figure in comparative historical context, but nevertheless significant in a country where such purchases could be unconstitutional. The correlation with state ownership expected from previous tables is also present in mandatory purchases.

8. The State as Mediator

Under central planning, the state administration was the fount of contact enforcement and the arbiter of inter-enterprise disputes that enterprises were not able to resolve themselves. In the transition period, enterprises are removed from the hierarchical system, but the economy lacks the dense network of legal institutions and informal mechanisms for contract enforcement and dispute resolution that are characteristic of market economies. There is wide scope for costly transactional failures.[22] For better or worse, state officials have the power to step into this breach, providing dispute resolution services.

Our survey asked enterprises to indicate the importance of a variety of mechanisms used by enterprises in the two previous years for solving disputes with their customers of suppliers. Among the mechanisms were other (i.e., third party) enterprises, banks, government, courts, private arbitration, and private security enterprises (the latter taken to include organized crime.) Formal court proceedings were by the far the most used alternative, with government the next most common.

Table 12 summarizes important elements of enterprise responses on dispute resolution, contrasting the use of the courts and of government in resolving disputes with the chief private sector alternative. The use of government intervention to resolve disputes is correlated with state ownership. Nevertheless, more than one quarter of fully privatized enterprises had been the recipient of such government intervention.

Table12 - PERCENTAGES OF ENTERPRISES USING VARIOUS METHODS OF DISPUTE RESOLUTION

Set of enterprises	Percentage of enterprises reporting the use various methods of resolving disputes with their suppiiers or customers		
	Intervention of government	Use of courts	Use of private methods (arbitration, security firms, etc)
All	38.2	61.0	23.2
No state ownership	28.1	61.2	23.7
Minority state ownership	41.9	51.6	19.4
Majority state ownership	55.3	64.5	23.7

9. Conclusion: A Cohesive State Sector?

We have shown that the intensity of many of the interactions between the state and enterprises is related to the degree of state ownership. This observation raises the question whether enterprise-state interactions are concentrated into a narrow set of enterprises, rather than being spread across the privatized sector.

To examine the degree of concentration of enterprise-state inter-relations, we compiled simple summary data on the total number of interactions between each enterprise and the state. Twenty-one possible interactions were examined among those listed above. In choosing the specific interactions to examine, two criteria were used. First, the interaction should clearly be one that is state promoted, rather than enterprise initiated, in order focus on government intervention. Second, there should be no double counting, through the inclusion of different reports of the same activities. Even given this second criterion, one would not expect a single enterprise to exhibit all of the interactions, since many activities, such as different forms of subsidy, are substitutes for each other.

Table 13 summarizes the pertinent information. Enterprise-state interactions are heavily concentrated in enterprises that have some state ownership. While 72% of completely private enterprises have three or fewer interactions, fully 82% of enterprises with majority state ownership had four or more interactions. This is strongly suggestive of a policy mechanism that is conscious of ownership when decisions are made on specific interventions into the enterprise sector. This conclusion is buttressed by the observation that those interventions most correlated with ownership are explicit state activities (state loans, funding of investment projects) rather than measures channeled through more independent bodies such as the commercial banks (or even the tax authorities.)

Table 13 - THE INTENSITY OF ENTERPRISE CONTACTS WITH THE STATE

	Percentage of enterprises with the following numbers of contacts with the state:				
Set of enterprises	0	1, 2, or 3	4, 5, or 6	7, 8, or 9	10, 11, or 12
All	4.8	50.2	35.3	8.0	1.6
No state ownership	7.9	72.1	19.3	0.7	0.0
Minority state ownership	3.2	32.3	64.5	0.0	0.0
Majority state ownership	0.0	17.9	52.6	24.4	5.1

These results stand in contrast to some widely held assumptions about the transition environment and to observations on other transition countries. Certainly, after mass privatization in Mongolia, state behavior does not conform to the assumption of the disinterested owner that has been commonplace (Aghion, Blanchard, and Burgess 1994, p.1328.) The results also indicate that there is a stronger correlation between ownership and interaction with the state in Mongolia than has been observed in Russia, for example (Commander, Fan, and Schaffer, 1996, p. 8.) In contrast to Stark's (1996, p. 126) observation that property transformation has resulted in the blurring of boundaries between public and private in Hungary, the data presented above suggest an increasing delineation in Mongolia. Whereas Rona-Tas (1996, p. 23) concludes that ownership is irrelevant in the interactions between the Czech state and Czech enterprises, our results suggest that ownership is important in Mongolia.

The question that naturally arises is what mechanism leads to the systematic pattern of interactions identified above. There are several possibilities. First, the enterprises that have residual state ownership might have different characteristics than others, and it is these characteristics that are important rather than state ownership per se. Second, legal constraints on the exercise of state power might cause the state to focus its attentions on those enterprises where it has an owner's power. Third, informal norms might be already in place, guiding interventions toward those enterprises for which the symbol of state ownership gives sanction to state intervention. Fourth, and relatedly, the observed pattern of enterprise-state interactions might result from paternalistic patterns of behavior between subordinate enterprise and superior bureaucratic owner (Kornai 1992b, p. 144). Lastly, following Shleifer and Vishny (1994), the presence of state ownership might alter the financial incentives of the state and of management. None of these hypotheses is inconsistent with the others, but it remains to be seen which one can most adequately explain the results that have been presented. This is the subject of further research.

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Notes

[1] See Pistor and Turkewitz (1996), Brom and Orenstein (1994), and Earle, Frydman, and Rapaczynski (1993 p. 17).

[2] In contrast to the conclusions of Aghion, Blanchard, and Burgess (1994, p.1328) and Fan and Schaffer (1993 p. 5) on other transition countries.

[3] This section provides only the information necessary for an understanding of the general context in which the paper's results should be place. A detailed overview of Mongolian privatization appears in Korsun and Murrell (1995).

[4] Before shares were offered to the general public, employees had the option of buying shares at the nominal opening price, which was based on the book value of net assets. Ultimately, this concession was rather unimportant since the opening prices tended to be above the auction prices and since the families of employees were not allowed to participate in the concessionary deals, thus limiting each employee's concessionary purchases to those shares that could be bought with the employee's own vouchers. The overwhelming majority of employee ownership resulted from employee participation in the auction process, just as any citizen participated in that process.

[5] See Boone (1994) for discussion of stabilization and Murrell, Dunn, and Korsun (1996) for the development of price liberalization.

[6] Table 2 omits data on one enterprise, which is very large compared to all other enterprises and which has very large state ownership. Inclusion of this enterprise would tend to obscure the general picture analyzed in that Table.

[7] Some enterprises did not submit 1994 accounts, necessitating the use of inflation-adjusted 1993 values for these enterprises.

[8] This was due to changes in relative valuations: the state did not sell any shares in already-privatized enterprises at this stage.

[9] See Korsun and Murrell (1996) for an investigation of the determinants of state ownership based on a much smaller set of enterprises.

[10] Their existence was mandated only in July 1993, after amendments were passed to the Economic Entities Law.

[11] Article 54, Clause 1, part 1 of the Partnership and Company Law of Mongolia of 1995.

[12] Comparison with other transition countries suffers from the lack of comparable published data. Pistor and Turkewitz's (1996, p. 225) summary of representation in the Czech Republic seems comparable to the situation in Mongolia. Blasi and Shleifer (1996, p. 89) found that 13% of the members of a small sample of Russian boards were state officials, a figure that is almost exactly the same as Table 3's 13.1% figure for government officials in an official capacity on boards of representatives. For Russia, Frydman, Pistor, and Rapaczynski (1996, p. 208) report almost the same figure as we do (46.4%) for enterprises that have at least one state representatives on their boards of directors. Given that residual state ownership after privatization in Russia is lower than in Mongolia, this suggests that the Russian state has been more persistent in securing representation on the boards of wholly privatized companies than has the Mongolia state.

[13] Government loans are viewed as subsidies, since these usually involve low interest rates and uncertain repayment.

[14] Blanchard (1994 p. 1170) identifies the main source of hidden subsidies in Poland appears as bank loans.

[15] In Poland, state enterprises have better access to loans (Belka et al 1994 p. 30) while in Russia there appears to be equal access for state and privatized enterprises (Fan, Lee, and Schaffer, 1996, p. 159.)

[16] The data on state loans probably overstate the flow problem, since many of these loans are from previous years.

[17] Fan, Lee, and Schaffer (1996, p. 143) report no correlation between the loan source and ownership type in Russia.

[18] The question used 'unfortunate market conditions' as the cause of the enterprise's problems, rather than any wording that could have been taken to imply that the enterprise was responsible for its plight, to remove any ethical content from the answers. Similarly, we focused on employment as the objective of the government aid, to reduce the negative connotations from admitting the receipt of such aid. Employment maintenance is also a likely goal of governments in transition environments.

[19] As far as one can judge from non-comparable data, Mongolia lies between Poland and Russia, in terms of soft budgets. Pinto et al (1992, p. 31) and Pinto et al (1993 p. 243 found essentially no expectation of government help in Poland, while Fan and Schaffer (1993 p. 36) and Sutela (1994 p. 424) report widespread soft budgets for Russia in 1993.

[20] The subsidies reported in Table 6 overlap with those in Tables 7-9, so that it would be double counting to accumulate all the arrangements listed in these tables.

[21] The questions sought information on government involvement, whether or not the government was the ultimate consumer.

[22] See Hendley et al (1997) for a description of such problems in Russia.

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