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Competitive Pressure from Neighboring Markets and Optimal Privatization Policy*

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Abstract

We formulate a mixed oligopoly model in which one state-owned public enterprise competes with n private firms in the same market and m private firms in the neighboring market. We investigate how n and m affect the optimal degree of privatization. The optimal degree of privatization is increasing with the number of private firms in the same market, and the relationship between the optimal degree of privatization and the number of private competitors in the neighboring market is an inverted U-shape. Our result suggests that more pressure from competitors supplying differentiated products can reduce the optimal degree of privatization. We also find that the optimal degree of privatization can increase with the foreign ownership share in private firms in the neighboring market.

JEL classification numbers: H44, L33, L44

Key words: market competitiveness, partial privatization, number of private firms.

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