

Machiavellian Underpricing

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Abstract

We analyse politically motivated privatization design in a bipartisan environment where politicians lack commitment power. Suppose the median class voters a priori favour redistributive policies. If the privatization programme succeeds in allocating enough shares to these citizens, they become averse to redistributive policies, which would be detrimental to the values of their shareholdings. To induce the median class voters to buy enough shares to shift their political preferences, underpricing is often necessary. The more unequal the society, the poorer the median class, the less willing they are to buy shares, the larger the necessary underpricing. When inequalities are large this leads to voucher privatization. Shifting the preferences of the middle class by privatizing is impossible when strong ex-ante political constraints require large upfront transfers to insiders, reducing the value which may be distributed through the privatization programme, or when social inequality is extreme.

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