

Navarra Center for International Development



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### **PRIVATIZATION IN A POLLUTING INDUSTRY IN THE PRESENCE OF FOREIGN COMPETITION**

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**Privatization in a polluting industry in the presence of foreign competition**

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**ABSTRACT**

Recent evidence shows that developing countries and transition economies are increasing privatizing their public firms at the same time experiencing rapid growth of inward foreign direct investment (FDI). In an international mixed oligopoly, we analyze the interaction between privatization and FDI in the context of environmental pollution and regulation. We find that the FDI incentive generally increases with privatization. Under export, welfare increases with privatization calling for complete privatization. However, under FDI due to the increasing pollution effect resulting from the relocation, the optimal degree of privatization is partial. If the degree of privatization that is required to attract FDI is very high, such that the welfare under FDI is lower than the welfare under export, the host country will deter FDI through lower degree of privatization.

**Keywords:** Emission taxation, Foreign Direct Investment, Trade, Privatization

**JEL Classification:** F12, F18, F21, L33, Q50, Q58

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