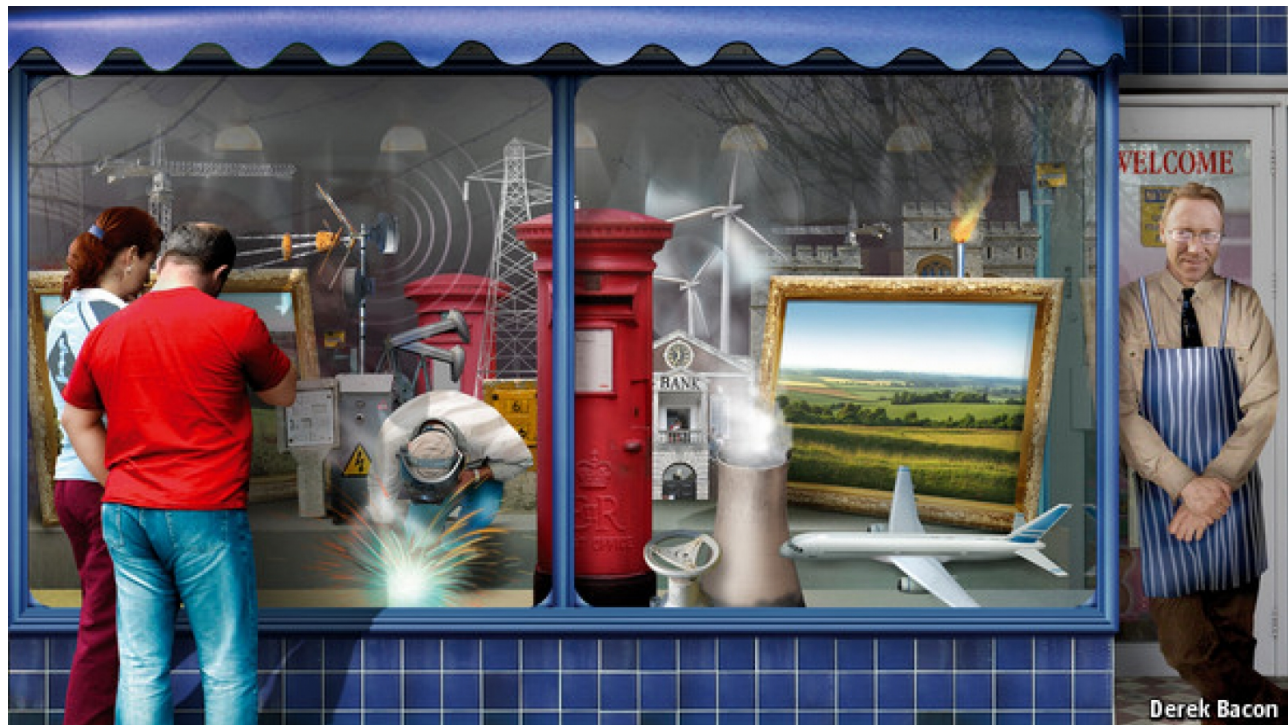


State-owned assets

Setting out the store

Advanced countries have been slow to sell or make better use of their assets. They are missing a big opportunity



Print edition | Briefing

Jan 11th 2014 | NEW YORK

THE past quarter of a century has seen several bursts of selling by the world's governments, mostly but not always in benign market conditions. Those in the OECD, a rich-country club, divested plenty of stuff in the 20 years before the global financial crisis. The first privatisation wave, which built up from the mid-1980s and peaked in 2000, was largely European. The drive to cut state intervention

under Margaret Thatcher in Britain soon spread to the continent. The movement gathered pace after 1991, when eastern Europe put thousands of rusting state-owned enterprises (SOEs) on the block. A second wave came in the mid-2000s, as European economies sought to cash in on buoyant markets.

But activity in OECD countries slowed sharply as the financial crisis began. In fact, it reversed. Bail-outs of failing banks and companies have contributed to a dramatic increase in government purchases of corporate equity during the past five years. A more lasting feature is the expansion of the state capitalism practised by China and other emerging economic powers. Governments have actually bought more equity than they have sold in most years since 2007, though sales far exceeded purchases in 2013.

Latest updates

In Belgium, arguments about Islam grow louder
ERASMUS

Donald Trump accuses Iran of violating the nuclear deal
DEMOCRACY IN AMERICA

Chicago's soda tax is repealed
DEMOCRACY IN AMERICA

[See all updates](#)

Today privatisation is once again “alive and well”, says William Megginson of the Michael Price College of Business at the University of Oklahoma. According to a global tally he recently completed, 2012 was the third-best year ever, and preliminary evidence suggests that 2013 may have been better (see chart 1).

However, the geography of sell-offs has changed, with emerging markets now to the fore. China, for instance, has been selling minority stakes in banking, energy, engineering and broadcasting; Brazil is selling airports to help finance a \$20 billion investment programme. Eleven of the 20 largest IPOs between 2005 and 2013 were sales of minority stakes by SOEs, mostly in developing countries. By contrast, state-owned assets are now “the forgotten side of the balance-sheet” in many advanced economies, says Dag Detter, managing partner of Whetstone Solutions, an adviser to governments on asset restructuring.

They shouldn't be. Governments of OECD countries still oversee vast piles of assets, from banks and utilities to buildings, land and the riches beneath (see table). Selling some of these holdings could work wonders: reduce debt, finance infrastructure, boost economic efficiency. But governments often barely grasp the value locked up in them.

The picture is clearest for companies or company-like entities held by central governments. According to data compiled by the OECD and published on its website, its 34 member countries

had 2,111 fully or majority-owned SOEs, with 5.9m employees, at the end of 2012. Their combined value (allowing for some but not all pension-fund liabilities) is estimated at \$2.2 trillion, roughly the same size as the global hedge-fund industry. Most are in network industries such as telecoms, electricity and transport. In addition, many countries have large minority stakes in listed firms. Those in which they hold a stake of between 10% and 50% have a combined market value of \$890 billion and employ 2.9m people.

The data are far from perfect. The quality of reporting varies widely, as do definitions of what counts as a state-owned company: most include only central-



Plenty to browse

2013 or latest, \$trn
Ranked by assets as % of gross debt

	GDP	gross debt	non-financial assets	value of state-owned firms*
South Korea	1.2	0.4	1.3	0.20
Australia	1.5	0.4	1.4	0.02
Norway	0.5	0.2	0.2	0.29
France	2.7	2.6	2.5	0.28
Italy	2.1	2.7	1.6	0.23
Germany	3.6	2.9	1.6	0.13
United States	16.7	17.7	10.3	0.06
Britain	2.5	2.3	1.2	0.12
Japan	5.0	12.2	6.6	0.48
Switzerland	0.6	0.3	0.1	0.04
Sweden	0.6	0.2	na	0.18
Canada	1.8	1.6	0.7	0.03

Sources: IMF; OECD *Including minority stakes

government holdings. If all assets held at sub-national level, such as local water companies, were included, the total value could be more than \$4 trillion, reckons Hans Christiansen, an OECD economist.

Moreover, his team has had to extrapolate because some OECD members, including America and Japan, provide patchy data. America is apparently so queasy about discussions of public ownership of commercial assets that the Treasury takes no part in the OECD's working group on the issue, even though it has vast holdings, from Amtrak and the 520,000-employee Postal Service to power generators and airports. The club's efforts to calculate the value that SOEs add to, or subtract from, economies were abandoned after several countries, including America, refused to co-operate.

Privatisation has begun picking up again recently in the OECD for a variety of reasons. Britain's Conservative-led coalition is focused on (some would say obsessed with) reducing the public debt-to-GDP ratio. Having recently sold the Royal Mail through a public offering, it is hoping to offload other assets, including its stake in URENCO, a uranium enricher, and its student-loan portfolio. From January 8th, under a new Treasury scheme, members of the public and businesses will be allowed to buy government land and buildings on the open market. A website will shortly be set up to help potential buyers see which bits of the government's £337 billion-worth of holdings (\$527 billion at today's rate, accounting for 40% of developable sites round Britain) might be surplus. The government, said the chief treasury secretary, Danny Alexander, "should not act as some kind of compulsive hoarder".

Japan has different reasons to revive sell-offs, such as to finance reconstruction after its devastating earthquake and tsunami in 2011. Eyes are once again turning to Japan Post, a giant postal-to-financial-services conglomerate whose oft-postponed partial sale could at last happen in 2015 and raise {Yen}4 trillion (\$40 billion) or more. Australia wants to sell financial, postal and aviation assets to offset the fall in revenues caused by the commodities slowdown.

In almost all the countries of Europe, privatisation is likely “to surprise on the upside” as long as markets continue to mend, reckons Mr Megginson. Mr Christiansen expects to see three main areas of activity in coming years. First will be the resumption of partial sell-offs in industries such as telecoms, transport and utilities. Many residual stakes in partly privatised firms could be sold down further. France, for instance, still has hefty stakes in GDF SUEZ, Renault, Thales and Orange. The government of François Hollande may be ideologically opposed to privatisation, but it is hoping to reduce industrial stakes to raise funds for livelier sectors, such as broadband and health.

The second area of growth should be in eastern Europe, where hundreds of large firms, including manufacturers, remain in state hands. Poland will sell down its stakes in listed firms to make up for an expected reduction in EU structural funds. And the third area is the reprivatisation of financial institutions rescued during the crisis. This process is under way: the largest privatisation in 2012 was the \$18 billion offering of America’s residual stake in AIG, an insurance company.

Parking meters, anyone?

State-owned entities regularly invest in other countries’ privatisations: sovereign-wealth funds were among the investors in Royal Mail, for instance. In many cases, governments will want to hold on to blocking stakes—typically 25%—in companies they consider “strategic”. Sometimes the law obliges them to do so. That will not necessarily deter potential investors, who can enjoy good returns even from companies with small public floats. From 2001 to 2012 the overall stock returns of listed SOEs in Europe, the Middle East, Africa and Latin America outperformed their benchmark indices, according to Morgan Stanley. This reflects the sharing of rents in sectors where, for a time at least, competition is limited, says Aldo Musacchio of Harvard Business School, co-author of “Leviathan Evolving”, a forthcoming book on state capitalism.

In America, even partial sales of federal assets can be a political minefield. When President Barack Obama suggested selling the Tennessee Valley Authority, an

electricity provider, even prominent Republicans squealed in protest, claiming that it would make power more expensive—but also seeming to want to cling on to this Rooseveltian relic for its own sake.

There is more activity at the state and local level, particularly in infrastructure projects, though much of this involves privatisation of management, not ownership, through the offering of long-term concessions to build and operate toll roads, bridges and the like. A decade ago such public-private partnerships (PPPs) were rare, but more than 30 states have now passed laws allowing them. Private operators have been taking over management of other assets, too, from parking to lotteries.

However, these transactions are not always well structured. Although it brought in \$1.2 billion up-front, Chicago's sale of a 75-year concession to manage its parking meters in 2008 is widely viewed to have been a lousy deal for the city. PPPs have a mixed record in Britain, too, though the Conservative-led government wants to do more and has even tried—so far without success—to privatise management of its defence-procurement arm.

What lies beneath

The greatest untapped opportunities may lie in land, buildings, subsoil resources and other “non-financial” assets. However, their scale is hard to gauge because of poor data-collection and accounting. Of the 35 countries that provide data on such assets to the International Monetary Fund, the OECD and Eurostat, only 16 report all categories, according to an IMF report. Some countries do not even record properties, let alone value them. Greece is a particular offender.

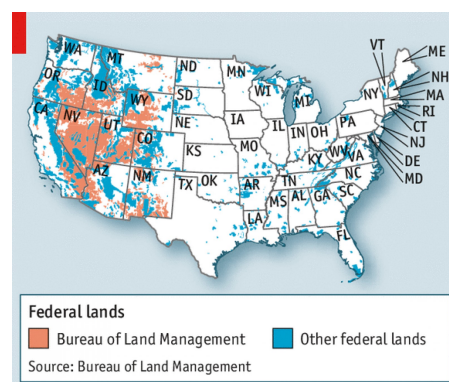
The picture is generally murkier still at regional level. Portugal's experience is not untypical: a decade ago it passed a law requiring its local authorities to value their property, but some have still not done so and methodologies differ among those that have. Local politicians often drag their feet, fearing that greater transparency will usher in painful rationalisation. This matters, because local and regional

administrations hold most of the non-financial sovereign assets in some of the largest economies.

In America, by contrast, the situation may be worse in Washington, DC, than in the states. The federal government lacks a detailed inventory of its buildings, points out Leonard Gilroy of the Reason Foundation, a think-tank. Management of these assets has improved a bit since the creation in 2004, by executive order, of a council to push reform in this area. But there is still far to go, as shown in a series of reports from the Government Accountability Office. One, in 2011, estimated that in 2009 at least 45,000 government buildings were under-used or unneeded.

America also has, for historical reasons, vast swathes of federally owned land concentrated in the West (see map). The Department of the Interior oversees more than 500m acres, around a fifth of the land area of the country. In fiscal 2011 its agencies spent \$13 billion more than they collected for use of land and resources—a deficit that critics want to see closed through better management or land sales.

One possibility, other than selling to individuals or developers, would be to sell to non-profit conservation trusts. These have mushroomed over the past decade: there are now 1,700, some handsomely funded, supported by hundreds of thousands of volunteers. Another approach would be to transfer ownership to state administrations, which have generally been more creative than the feds in their management of parks, grazing land and buildings, says Chris Edwards of the Cato Institute, a libertarian think-tank. A study conducted for a land-management task-force in Nevada (which is 84.5% government-owned) concluded that state-managed land generates net revenue of \$6.29 an acre on average, compared with a net loss of \$1.86 for federally managed land. However, both ranchers and greens support the status quo.



The greatest value could lie beneath. The Green River Formation, a field of sedimentary rock beneath Colorado, Utah and Wyoming, contains the world's largest deposits of oil shale. Three-quarters of this is under federally controlled land. Leases from oil- and gas-fields under federal land could potentially generate royalty, rent and bonus payments of \$150 billion (excluding operators' tax payments) over ten years, according to the Congressional Budget Office. Up to now, almost all of the shale-oil and gas revolution in America has taken place on private land.

Putting a value on public-sector bricks, mortar and soil is tricky. The IMF paper sheds some light, though its authors load their findings with caveats because of national differences in coverage and valuation techniques. They estimate that non-financial assets average 75% of GDP in advanced economies, though levels range widely, from 40-50% in Canada and Germany to 120% in Japan (see chart 2). In most countries, these are worth more than financial assets (stakes in listed firms, sovereign-wealth and securities holdings and the like). The value of the two combined is typically more than half gross public debt.

In 2011 economists at UBS estimated that some euro-zone countries' public fixed assets (land, buildings, plant) were worth two to three times more than their financial assets. The bank reckoned that fixed assets held by euro-zone central governments alone could be worth €4 trillion, net of depreciation—far above the value of their state-owned companies, and even exceeding that of state-owned corporate assets across the entire OECD.



Cathedral for sale: €1

France, with its wealth of public buildings on prime sites, has the highest concentration of state-owned property in Europe.

According to government financial statements for 2012, property directly owned by the French state is worth €190 billion. Of this, €54 billion is valued at fair market value because it is deemed either to have a use that is not specific to the state or to be easily convertible (eg, into offices, shops or housing). The remainder is valued either at cost, at discounted replacement cost (for prisons) or at a symbolic value for monuments and other historic buildings (for instance, €1 for each of the 96 cathedrals transferred from the Catholic church to the state a century ago). “Land represents only 4% of value of the total portfolio held by the state, which suggests it is underestimated,” says Arnaud Burillon, a property expert with PwC.

Moreover, the €190 billion does not include property owned by hundreds of state-controlled operators, including museums, palaces and the National Forest Office, which controls around 11.6m acres. Their portfolios were appraised at a modest €42 billion in 2009. Nor does it include properties held by local authorities: 37,000 municipalities, 101 departments and 22 regions. In addition to their administrative offices, these authorities own schools, hospitals, retirement homes and more, and none of these institutions has to produce a balance-sheet.

Even in countries with reputations for public-sector openness, estimates can only be rough. To calculate the overall market value of sovereign assets in Sweden, Jorgen Sigvardsson, also of PwC, used a methodology that extrapolates from property-tax values (and thus excludes untaxed property, such as historic buildings). His estimate: a total of \$230 billion in 2009, of which property accounted for \$100 billion-120 billion and corporate assets (including the state’s stakes in Telia Sonera and SAS) for \$90 billion. If his number-crunching is accurate, and if state-owned property accounts for a similar share of the economy elsewhere, OECD governments own land and buildings worth some \$9 trillion, equivalent to 18% of their general government gross debt.

Britain, too, has done more than most to catalogue and appraise its holdings. Every few years it publishes a National Asset Register. The latest, in 2007, contained 1,110 pages of tables, including breakdowns of the estimated value of each government

department's tangible fixed assets (including heritage sites), intangibles (such as software licences) and shareholdings. It assigns value to holdings as minor as the dormitory at Woodbridge Airfield—worth £2.8m, since you ask. That is a mere speck on the Ministry of Defence's balance-sheet: its tangible assets are £70.4 billion, a quarter of the total for all government departments. Local-authority assets are totted up separately. As of March 2012, authorities in England alone had fixed assets of £234 billion, 75% of which were land and buildings, including public housing.

Few countries display such attention to detail. Ian Ball, former head of the International Federation of Accountants (IFAC), points out that many countries do not even know the book value of their assets, let alone the market value, because they lack information to calculate depreciation. Most make do with “cash basis” accounting rather than the “accrual” accounting used in the private sector. This helps obscure weak finances, because costs are counted only when the bill comes due, not when the obligation is incurred. And if there is no cost of capital associated with, say, ministry offices, there is less pressure to use them efficiently or dispose of them.

IFAC has led a crusade to get countries to adopt a public-sector version of the IFRS accounting rules used by many large companies. This standard, known as IPSAS, has been adopted in full or in part by Britain, France, Canada and New Zealand, among others. Germany is holding out.

New Zealand probably comes closest to managing assets as a company would, in some respects going even further: it not only uses the accrual method but updates its financial statements each month. It even imposes a capital charge on government departments for properties and their contents, payable to the treasury. This has encouraged some selling of art and of under-used buildings. “It's not popular with the civil servants, but it has focused minds,” says Mr Ball.

Now leasing, Place de la Concorde

Some public buildings will always be off-limits: no crisis is big enough to warrant the sale of the Parthenon. But government offices and diplomatic buildings are ripe for rationalisation. Activity is picking up, mostly in markets where dizzying price rises have made staying on prime sites hard to justify. More than a dozen foreign missions in London, including the Dutch and American ones, are cashing out and moving to less fancy (sometimes safer) districts, or considering doing so. Canada's High Commission building on Grosvenor Square was sold last November for £306m. The buyer, an Indian developer, plans to turn the grand building into luxury flats.

Leasing can generate efficiencies, too. France, for instance, has leased out a defence-ministry building on the Place de la Concorde, moving its occupants to less plush offices on the outskirts of Paris. Leasing provides a steady stream of revenue that can help trim annual deficits, as opposed to the one-off debt-reducing pop that comes from a sale. It can also be an attractive option for financially troubled countries that would struggle to obtain fair value in a disposal, because investors would know it was a fire sale.

Though governments are increasingly considering reforms to streamline public administrations, receipts and savings have been modest so far. Governments often fear stirring up controversy over assets that have a place in the public's heart. The brouhaha can reach a level that forces deals to be undone. Sweden reversed the sale of its forests after an outcry over public right of access; Britain pulled back, also after a public outcry, from trying to sell off Forestry Commission land in 2010.

Privatisation is not always possible, or desirable. Keeping land in state hands is sometimes the only way to protect vulnerable landscapes, plants and wildlife. Proceeds from sales have



to be balanced against the loss of future revenue (if the assets are a source of income) and even, in some cases, social cohesion. Sometimes it pays to wait: in industries such as transport and utilities, prices for consumers may rise sharply because of insufficient competition if regulations are not overhauled before assets are sold.

The Shareholder Executive, an arm of the Department for Business, Innovation & Skills, controls some of Britain's largest state holdings (though not the stakes in bailed-out banks, which are held at arm's length by the Treasury). Mark Russell, its chief executive, favours privatisation, but says there should be no rush to sell holdings that are "deemed to be a good" and in which "greater efficiency can be achieved at marginal cost to the taxpayer", he says. He cites Companies House, the national corporate registry, as an example.

Assets that remain state-owned in Britain will be in better hands than they were in the past, Mr Russell argues. Before his unit was set up a decade ago, holdings were typically scattered among different government departments, with civil servants providing much of the advice. Now they are under one roof, overseen by teams with corporate-finance and private-equity backgrounds. The Shareholder Executive is partly modelled on the highly regarded sovereign-asset managers in Nordic countries. Their approach is characterised by a clear separation of ownership and management (to avoid the government acting as both market participant and regulator), private-sector-style openness (along with the short-termism) and a firm but not intrusive role in governance.

Such shake-ups will, in any case, often lead naturally to sell-offs over time. In the late 1990s Sweden's Social Democrats launched a plan to rationalise, but not sell, state assets. The overhaul, led by Mr Detter, exposed the superfluity of many SOE subsidiaries and other holdings, spurring the government to put three times more under the hammer than the nominally more privatisation-friendly previous administration had done.

All of which points to a huge opportunity for governments to sell or sweat more assets, and by doing so reduce fiscal stress. With political courage and some imaginative structuring of transactions, they should be able to lay to rest the widely accepted idea that their boldest moves are already behind them.

Correction: An earlier version of this article stated that the National Forest Office in France controlled 4.5 billion acres. The figure is 11.6 million acres. This was changed on January 11th.

You've seen the news, now discover the story

Get incisive analysis on the issues that matter. Whether you read each issue cover to cover, listen to the audio edition, or scan the headlines on your phone, time with *The Economist* is always well spent.

Enjoy 12 weeks' access for \$12

