TRANSPARENCY

OF

STATE COMMERCIAL ASSETS

THE FORGOTTEN SIDE OF GOVERNMENT BALANCE SHEET

by Dag Detter

INTRODUCTION

Government debt is a fully transparent securitytraded on the capital market, with its rating acting as a health indicator of government financesfor the whole world to see. In contrast to this widely scrutinised and debated side of the balance sheet, the assetside and then especially commercial assets are more or less hidden in black box without even the government having a complete picture of its contents, value or performance.

A few years ago this assets class have might have been dismissed as irrelevant. However, in today's economic environment, it has become obvious that many governments around the world have a substantial portfolio of commercial assets yielding often a very small return to its ultimate owner - the taxpayer.

This under utilized assets class has become a potential tool to help clear up unproductive bureaucracyand vested interests in order to create sustainable economic growth in India, as well as in Europe and even the US. Understanding these assets and putting them on an equal footing in a transparency perspective to that of listed companies seems then an obvious requirement.

THE FORGOTTEN ASSET CLASS

State-owned Commercial Assets ('SOCAs') are probably one of the largest asset classes globally, worth many times over the value of private equity and hedge funds put together. These forgotten assets are less visible and often lacking professional management, but with an almost unlimited upside if managed correctly.

Worldwide their total value is estimated well over USD 12 trn, or representing 20 per cent of global GDP in value terms. However, in some BRIC-countries such as India and China it could be more than half of GDP.Even in the US there is a wide range of state-owned commercial assets, including US Postal Services, Amtrak, commercial banks and financial institutions, as well asa vast portfolio of commercial real estate held by state or local governments.

These vital assets have the potential to affect our lives both as taxpayers and through their effect on the development of the global economy, as they are the suppliers of fundamental services such as energy, transportation and finance. Noeconomycan really afford poor performance of such key infrastructure and compensate the drag they have on the economy with taxes?

Privatisation is the instinctive response from a financial perspective when putting the spotlight on commercial assets owned by a government. Regardless if we are seeing these assets as something to be sold or kept and managed professionally, it requires proper transparency.

PROFESSIONAL AND ACTIVE OWNERSHIP

The concept of a state acting as a professional owner is not new.Singapore, Finlandand many others have shown how to organise these assets in a separate portfolio with a commendable transparency level.In addition, National Wealth Funds such as Temasek and Mubadala of Singapore and Abu Dhabihas also added a debt rating to improve the transparency of the portfolio.

Following the financial crisis in the 90's,Sweden led the way as one of the firstcountries to actively manage its portfolio of commercial assets, including restructuring the postal services, railways, electricity and telecoms to become one of the mostproficient in Europe. Improving accounting and reporting standards was an obvious and fundamental pillar in the restructuring of a portfolio representing around 25 per cent of GDP in value terms. As a resultprofits materialised within a year and the value of the portfolio quickly outperformed the local stock market.

PUBLIC ASSETS, PUBLIC INFORMATION

Although many of these assets may not be listed on a stock exchange, they are public companies in the purest sense and should therefore be even more transparent than listed companies.

Transparency for state-owned commercial assets transparencystarts by deciding what is considered as commercial assets, i.e. what activities are, or could be subject to market forces. Apart from the obvious deregulated activities, commercial real estate and also commercial forestry assets are some assets often overlooked in this context.

Once selected these assets are often centralised under a common ownership management. However, even if the assets are maintained under a decentralised management and ownership, it should be reported as if a virtual holding company with a coherent transparency policy.

INITIAL ANALYSIS - IN A FEW MONTHS

The first step is an aggregated annual review simply outlining the total list of assets deemed to be commercial assets, as well as a breakdown of the perhaps five largest sectors often including finance, energy, telecom, transportation, real estate and forestry.

The information published about the portfolio is only the most basic in order to obtain an initial understanding of the portfolio on an aggregated level of its strategic, financial and economic potential. This would include, potential market value, profit, leverage, and dividend for the aggregated portfolio and by sector.

This exercise would only require a few months to finalise and publish.

Similarly, understanding the vast real estate portfolios often held by governments, to be included in the aggregated report,can be done in parallel and finalised within the same time frame of a few months. Apart from an approximate value of the real estate portfolio it would also be broken down into segments such as location, type,size, marketability etc.

CONSOLIDATED ANNUAL REPORT

The ultimate goal in transparency is naturally a consolidated annual report audited according to international standards, as well as quarterly reports to maintain a flow of information throughout the year.

Publishing a clear set of goals for each asset and their management, along with periodic assessments of how well they have achieved their objectives, as if they were privately held, is fundamental to good corporate governance. Hence, the quality of reporting and auditing should be of the highest international standards for each individual company as well as on an aggregated level for the entire portfolio.

ECONOMIC VALUE OF TRANSPARENCY

Open access to key information provides a basis for government accountability and limits the opportunity for self-serving policies. Without accurate and detailed information, it is difficult to assess company and board performance, set targets and allocate capital efficiently.

Political consensus is helpful when challenging the vested interests wanting to preserve the poor performance of the past and keeping these assets away from scrutiny in the future.

The current financial crisis is a uniqueopportunity, much to precious to waste. This is the timeto finallydemonstrate that the economic valueis indeed greaterthan the political costs of opening up this black box - to the benefit oftaxpayers, employees andthe world economy.

Dag Detter is the founder and Chairman of Detter & Co, a specialist advisor on state assets. He is the former President of Stattum, the Swedish state holding company and Director of State Enterprises within the Swedish government leading the restructuring of the Swedish commercial portfolio in the late 90's.