Country Specific Links
Other Links
PFM & Development Blogs
Macroeconomists' Blogs

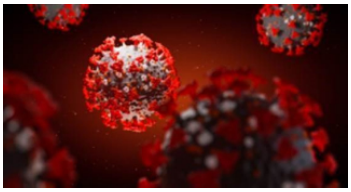
Translate Blog
Caution: automatic computer-generated translations

Search
Go

« Tackling Corruption in Governments' COVID-19 Health Responses | Main | The case for clarity in reporting of debt and fiscal risks »

November 16, 2020

How Government Equity Investments Can Help Boost the Recovery



Posted by Dag Detter, Stefan Folster and Josh Ryan-Collins [1]

As the second wave of the Covid-19 virus spreads across Europe, it is becoming clear that many firms in key sectors will be unable to generate the revenues needed to pay back the huge accumulation of corporate debt, much of it owed to, or underwritten by governments or central banks. Widespread defaults due to debt-induced insolvencies could lead not only to higher unemployment but would also damage the financial system, the public finances and the wider economy. Even firms who do not face redundancies or insolvency may be reluctant to invest for many years to come given the debt overhang and low prospects of growth.

Under such conditions, there is a strong case for governments to consider equity investment or debt-for-equity swaps, rather than further loans to keep viable firms afloat. In a new report for the UCL Institute of Innovation and Public Purpose (IIPP) we argue that public equity investments can succeed, provided that government ownership is institutionalized according to the highest standards of corporate governance and structured as politically independent 'Public Wealth Funds'.

An independent public wealth fund in this sense is a commitment device that can provide direction and confidence for investments in future industries at a time when there are huge pressures to do so but little risk appetite. Public investment on a large scale is needed to ensure that the recovery will support societal goals such as the transition to a zero-carbon economy, and deal with regional inequalities and housing affordability.

To some, such a move would be a dangerous step towards some form of state capitalism. However, high income economies already own public assets worth twice GDP. [2] The creation of new public wealth funds would result in only a fractional increase in such holdings and, over the longer term, could be much more cost effective than more debt financing. Such funds could also provide the opportunity for governments to steer the economy onto a more sustainable growth path.

Yet, how to govern public assets to generate value has received little attention compared to the vociferous debate over whether or not to nationalize or privatize these assets. If poorly managed, public equity bailouts risk throwing a wet blanket on growth prospects.

The holy grail of public asset management is an institutional arrangement that both removes governance from a government´s direct responsibilities, but at the same time encourages active commercial governance of public assets. The aim is to generate value for the public, and a dividend that can benefit society as a whole.

To this end, we suggest institutional structures that are highly transparent, insulated from day-to-day politics, have clear and simple goals, and are able to specialize in their respective area of expertise. Public investments must be targeted to avoid crowding out other firms or investors, while crowding in those that otherwise might be reticent to invest. Paraphrasing Keynes, the important thing is "not to do what others do a little better, but to do the things that are not done at all."

We believe that these principles can best be adhered to with Public Wealth Funds that are wholly publicly owned but at the national level separated into a National Wealth Fund in charge of mature assets; mission-driven venture capital funds focused on innovation, climate transition and regional growth; and at the regional level, Urban Wealth Funds to support housing and urban renewal.

Even assuming that the suggested equity investments loses their value, the direct fiscal cost of investing in the above mentioned funds would be small, only around 0.1 percentage points of GDP per year. Moreover, over time some of these investments would likely turn a profit. Historically, the yield on equity has been around 6 percent, while the cost of servicing public debt for the initial investment is negligible or even negative at current interest rates. If the entire portfolio of public assets were properly accounted for and professionally managed, they could potentially generate some 3% of GDP in additional revenues to government budgets.[3]

This could encourage policymakers to take into account the full spectrum of the public sector balance sheet by introducing basic tools such as accrual accounting and a focus on net worth as the most comprehensive fiscal measure.[[4]] These fundamental building blocks would help bring about greater transparency and disclosure, enabling governments to pursue optimal decisions with respect to the management of public assets to the benefit of society as a whole.

The report will be published by the IIPP on November 16.

This article is part of a series related to the Coronavirus Crisis. All of our articles covering the topic can be found on our PFM Blog Coronavirus Articles page.

[1] Dag Detter led the restructuring of the Swedish portfolios of public assets, the first European country to actively manage its Public Wealth and is the co-author together with Stefan Fölster of the *Public Wealth of Nations*. Stefan Fölster is the President of the Swedish Reform Institute and Associate Professor at the KTH Royal Institute of Technology in Stockholm. Josh Ryan-Collins is a Senior Research Fellow at IIPP.

[2] https://www.imf.org/en/Publications/FM/Issues/2018/10/04/fiscal-monitor-october-2018

[3] https://blogs.imf.org/2019/06/18/a-global-picture-of-public-wealth/

[4] https://blog-pfm.imf.org/pfmblog/2020/10/-how-better-management-of-public-assets-can-boost-the-recovery-.html

Note: The posts on the IMF PFM Blog should not be reported as representing the views of the IMF. The views expressed are those of the authors and do not necessarily represent those of the IMF or IMF policy.

How Government Equity Investments Can Help Boost the Recovery,&uri=https%3A%2F%2Fblog-pfm.imf.org%2Fpfmblog%2F2020%2F11%2F-how-government-equity-investments-can-help-boost-the-recovery-.html" class="first">Email this Subscribe to this feed Save to del.icio.us Digg This!
Posted by Blogmaster on November 16, 2020 | Permalink

Comments

Post a comment

Comments are moderated, and will not appear until the author has approved them.

If you have a TypeKey or TypePad account, please Sign In

(You can use HTML tags like <b> <i> and <ul> to style your text.)

Your Information

(Name and email address are required. Email address will not be displayed with the comment.)

Name

Email Address

Web Site URL

Post Preview

Back to top of page

Subscribe to our feed

November 2020

Sun	Mon	Tue	Wed	Thu	Fri	Sat
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30					

Nov 20

Recent Posts
Enhancing Government Effectiveness and Transparency: The Fight Against Corruption
The case for clarity in reporting of debt and fiscal risks
How Government Equity Investments Can Help Boost the Recovery
Tackling Corruption in Governments' COVID-19 Health Responses
Best Practices in Project Appraisal and Selection

Recent Comments
Srinivas Gurazada on A Stacked Layer Model Approach to PFM Digitization
David Fellows on A Stacked Layer Model Approach to PFM Digitization
Irek Smolewski on A Stacked Layer Model Approach to PFM Digitization
BZ on Fiscal Risks from Public Infrastructure
Elias Lopez on Why Sovereign Wealth Funds Should Not Invest at Home

Categories
Accounting
Aid
Anti-Corruption
Audit
Books
Budget
Budget Execution
Budget Rules
Budgetary Classification
Budgetary Coverage
Cash Management
Chart of Accounts (COA)
Debt Management
Development Agencies
Economic Growth
Employment
Events/Seminars
Fiscal Risks
Governance
IMF
Job offers
Local Government
Medium-Term Framework
Performance Budgeting
PFM Blog
PFM Reform
Political Economy
Public Financial Management
Public Investment
Public-Private Partnerships
References
Taxes
Transparency
Treasury
Uncategorized
World Bank