

Lessons for Government from Households' Investments Management

At any point in time a household has a collection of assets that it owns – a house, a car, an interest in Kiwisaver, or maybe a some shares or a rental property. Few people think of their portfolios as fixed forever.

Central government has a range of assets which is much more arbitrary. Leaving aside those that it would not contemplate selling, like roads, the government has a jumbled collection of assets that reflect history rather than an assessment of the government's needs in today's economy. The same is true of local government.

Who in their right mind would argue that the portfolios that central government and councils have ended up with make sense in the modern economy? It would be just as illogical to argue that the governments of the day, facing the same decisions again, should have held onto their shareholdings in Contact Energy and the Port of Tauranga.

Naturally, the sale of business activities would free up government capital for investment in other priorities. A stark case in point is Christchurch City Council, which owns 100 percent of a large construction business and is the majority owner of the port and the airport. Christchurch has massive capital needs for investment in infrastructure, schools and cultural assets. I have been waiting for someone to explain to me why it would not make sense to partially or fully sell some existing assets to help finance much-needed new investment requirements.

Like households, an alternative for government or councils is to raise additional debt to fund new investment. This would increase balance sheet risks for ratepayers. Ratepayers would have to meet the interest burden even if the Council failed to achieve an adequate return on its assets, and there are obvious reasons why they could fail. It is hard to see how extra debt can be justified, given the extent of the non-core assets the council holds.

Other owners are likely to be better able to assess, manage and absorb ownership risks than are ratepayers at large.

The same goes for the Auckland Council and Wellington City. They seem opposed, for instance, to any sales of large holdings in their ports or airports at a time when their mayors are pushing their ratepayers and central government to invest in otherwise unaffordable schemes like light rail and Absolutely Positively Wellington projects.

Likewise, it is imprudent and unnecessary for central government to have huge commercial investments in particular sectors, such as the energy sector – the electricity generators Meridian, Genesis and Mighty River Power plus Solid Energy and Transpower. Taxpayers would be less at risk if government took on less risk.

Of course, if assets are sold, it is important that the proceeds are used wisely. In the present environment the government is unlikely to use the proceeds to boost further operating spending that is already unsustainably high. Legislation could be clear on this point if it were regarded as a problem.

In summary, central and local government should adjust their asset portfolios, just as a households do from time to time, by partially or fully privatising businesses that they no longer need to own.

One problem with privatisation being virtually a taboo subject in the last decade is that public debate is much less informed than it needs to be, and public fears and concerns have not been adequately addressed.

The fear of overseas ownership is an important example. It should be no surprise or concern if foreigners end up owning some of the commercial assets sold by governments. Foreign ownership spreads risks and brings technological and management expertise and access to global markets.

A concern which an asset switching perspective puts to rest is the claim that when the government sells assets, more of New Zealand's assets end up in the hands of foreigners. For a start, it appears that New Zealand

investors, such as the New Zealand Superannuation Fund, ACC and private investment funds might be keen buyers of these assets.

Secondly, the government is to retain at least 51 percent ownership of the privatised assets, so control of the companies cannot go offshore. Thirdly, under a floating exchange rate there can be no net transfer of wealth between New Zealanders and foreigners from a competitive sale process. Foreigners must exchange their existing New Zealand assets (for instance cash) to participate in a partial privatisation of government assets. Unless New Zealanders as a whole want to increase their overseas investments, foreigners as a whole can only own a different portfolio of New Zealand assets.

For more on this and the many myths that have been allowed to grow around privatisation, and an outline of the broader benefits of partial privatisation that are not discussed above, check out my *Truth About Privatisation* series on my blog at RogerKerr.wordpress.com.

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