

Government Review of State Assets

Submission to the Review Group

**Irish Congress of Trade
Unions**

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Introduction: Taking the Broader Perspective.

A review of the commercial state companies undertaken on behalf of Government presents a good opportunity to take a long term, active review of the role of state companies in Ireland's wealth and job creation.

The Terms of Reference (TOR) for the Group are:

To consider the potential for asset disposals in the public sector, including commercial state bodies, in view of the indebtedness of the State.

1. To draw up a list of possible asset disposals.
2. To assess how the use and disposition of such assets can best help restore growth and contribute to national investment priorities.
3. To review where appropriate, relevant investment and financing plans, commercial practices and regulatory requirements affecting the use of such assets in the national interest.

The group is also to examine intangible assets, which include, *inter alia*, radio spectrum allocated for broadcasting and telecommunications; carbon emissions permits; and mineral, hydrocarbon and other licences issued by the state.

Congress urges the Review Group to take a wide interpretation of the very restrictive terms of reference set for the review. As three of the four terms of reference seem to lead to only one outcome, which is privatisation, the work of the Group is very constrained and the intended outcome may regrettably be a narrow privatisation agenda, with some possible restructuring of some of the companies.

These terms constrain what should be a serious and useful review of the potential of the companies. Therefore this Review should interpret its terms widely and attempt to see these major companies as developmental, from a long term perspective, not for some short term cash, in a fire sale. Their potential for jobs, wealth creation and strategic development has never been so vital now that several of the leading

private sector indigenous companies have collapsed. Three of the four terms of reference appears to mandate the course of privatisation, pre-empting a positive analysis and contribution from the group.

The second TOR appears to be contradictory as it asserts that privatisation of productive assets “can best help restore growth” when in fact it is likely to reduce it, particularly if the capital is used to pay bills. On the other hand, it also appears to rule out using the capital receipts from privatising to paying off day to day bills which is hopeful because it calls for the capital to “contribute to national investment priorities.” In short, the Group, in its infinite wisdom, is supposed to know what to recommend selling off less productive assets and to recommend that the state invest in more productive ones.

Congress urges the Review Group not to recommend the “low road” of sell-off of some of our state companies, for short term cash. Selling assets for revenue to pay off current expenditure rather than reinvest in capital assets is always a poor policy, whether it is for individuals or firms or nation states.

Turning productive assets into cash for short term reasons would be extraordinarily short-sighted. It is akin to selling the family silver to pay for bills, except that these assets are not ornaments, but productive. Yet that is what is being done.

The Balance Sheet Impact of Privatisation

It is perhaps an oversight that the TOR appear to show a lack of understanding of national balance sheets. If there is to be any change in Ireland’s Balance Sheet from privatisation, it will *reduce* it. Selling one productive asset for cash means no change – provided you get the full price and there are no major transaction costs. But today asset prices are depressed worldwide, so they will not get full value; privatisations are priced low to sell and transaction costs are high. Thus Ireland’s net position will be a reduction in its net assets.

We will get cash, but the government would be selling off productive assets to “spend” capital on day-to-day bills for one year, or pouring the cash into the hole that is Anglo Irish Bank. It can be argued that that cash will be used to pay off the national debt. But the capital from selling ESB, RTE, our ports and airports will go straight to the government-guaranteed speculators who lent to Anglo Irish, or to pay day-to-day expenses of government.

Is there a need for cash? NTMA reported that “the Exchequer is fully funded through to the first quarter of 2011.” Ireland has €20bn sitting in *cash* balances today and our Pension Fund is worth over €24bn. Furthermore, the National Debt will be close to the EU average at 87% of GDP at year end. But on the net Debt position will be only 38%. Interest on this debt is best paid off when we return to economic growth, not by liquidating capital assets in a time of decline or no growth.

Congress has pointed out that the performance of state companies has been very good for two decades. These companies have made major returns in cash dividends over the years and the sell off would both kill off this income stream and their developmental potential. Further, the cash receipts from those which were privatised far exceeded the state investment in them¹ – demonstrating the high valued added in their operations (but they were sold off in better times).

We believe that future privatisation is likely to be through a trade sale and not a share floatation. A sell-off on the stock market would be unpopular, after the lessons of Eircom, which the Irish public, at least, has learnt. A privatisation through a trade sale to another company either in the same business, or to an venture capitalist is most likely. Private equity firms would seek to extract the maximum in the shorter possible time, just like Valentia did to Eircom. These firms have absolutely no commitment to employees, to social or community or geographic interests.

¹ Sweeney found that total investment by the state in all companies totalled €1.5bn over the years, but privatisation receipts had generated €8.5bn to 2004, and the value of the remaining state companies was at least €7bn. (Selling Out: Privatisation in Ireland).

New Enterprise Paradigm

In the real economy, there has been a fundamental paradigm shift. This has yet to be fully grasped by many policy makers:

- Major, long-standing leading Irish private companies have collapsed, overnight.
- Their losses have been staggering and have endangered the state itself .
- The state – taxpayer - has bailed many of them out, and the full costs are yet unknown.
- More Foreign Direct Investment may shift, over time, to emerging economies.
- FDI has played a vital role in Ireland’s economy and will continue to do so, but we have to prepare for a possible decline over time.
- State-owned companies are performing well and are among the largest Irish indigenous companies.
- A number of indigenous Irish companies are major overseas investors .
- Therefore, we need to harness all performing indigenous enterprise, including the state companies, in the interests of the economy.
- Thus, selling off fine companies to pay bankers’ bills, no matter how large, would be very short-sighted. In fact, it would be counter to Ireland’s national interest.

There are clear differences between private and public sectors in every economy, but there is not the gulf between the two that many commentators portray. The recent demonisation of the public sector by many, including government politicians, was harmful, distorting and makes coherent policy formulation difficult.

For if we want sustained and productive reform of the public sector, we need a realistic assessment of its role, its interaction with the private sector, policy formulation *and* implementation. Many private firms are dependent on the public

sector for contracts and the cutbacks have deeply impacted upon these private firms and their managers and employees. There is a clear synergy between the two sectors and it should be recognised and built upon, consciously, to ensure the best of both sectors are enhanced.

This Review Group could have a role in developing such an approach, to the benefit of the economy and society.

The Interaction of the State and Enterprise is Complex, as we have learnt to our cost.

The Role of the State and Enterprise is complex, as we have learnt to our cost. But it is not that state firms are costing us a fortune in subsidies but that the top Irish private firms – namely the banks - failed and are costing taxpayers a great fortune. The taxpayer is bailing them out and will do so for decades. The Review should really be paralleled by another Review on Governance and Competence in the private sector.

Who would ever have forecast that the state in many western countries would take over the banking system, the car industry and many other parts of the “Commanding Heights of the Economy” in the early 21st century, so soon after the privatisations of the 1980s and 1990s?

The state “may appear to be withdrawing from the economy.... but it is simultaneously expanding into new areas like regulation and is establishing new operations and spheres of influence. The state grows and retreats over time from different areas of the economy.”²

Internationally, the role of a state in owning commercial companies is mixed. In some developing countries, corrupt governments manipulate the state companies they own and this has been a financial and economic failure, at worst for personal

² Sweeney, p 147, 2004

gain, while many other countries have had very successful state companies. There has been an inclination to use the companies as tools of government for diverse, unquantified policy objectives, including in Ireland, in the past. There has been considerable improvement in the governance of state companies worldwide, after rocky starts for many decades in developing countries.

The key to success is to have a clear, arms-length relationship between the state and the board of the company, with the state as a supportive, but not interfering shareholder and an independent board.

State companies will always be with us and this is recognised even by the OECD. The OECD has a comprehensive guide to the best form of governance of state owned companies³ which will apply less to those in Europe, than in the developing world.

The perceived superiority of private ownership over the state owned companies is questionable. Most studies found little difference in performance. However, even after the collapse of the "Commanding Heights" of the Irish economy of all of the privately owned Irish banks, some people still seem to think that state companies are inferior to privately owned ones. There is however, better governance through arms length operations improves performance further.

It should be noted that in most European countries, complex share ownership structures discourage hostile takeovers and even in the US, poison pills exist in companies to prevent these takeovers. Some are critical of this, believing that the constant threat of takeover is an "incentive" to better management performance. Others hold that it encourages corporate short-termism, which contributed much to the Crash of 2008. The point is that state ownership or part-ownership can be an asset in hostile takeovers - an asset which can and should be used with care.

³ OECD 2005, <http://www.oecd.org/dataoecd/46/51/34803211.pdf>

Minister Eamon Ryan was correct to challenge the ideology of “Public bad: private good” earlier this year. If anything, the reverse might be said to be true. The idea of a superior performance by the Irish private sector over the public sector has been deeply tarnished by bad behaviour by the golden circle in that sector in Ireland.

This Review should really be accompanied by a parallel Review on governance and competence in the private sector.⁴ The Anglo-American, “shareholder value” model of corporate governance model of private companies, which has been a major contributory microeconomic factor in the near collapse of the capitalist system should be radically changed to consider the roles of all stakeholders in companies rather than just shareholders. The myriads of connected companies within many large private groups, the use of offshore operations, of unlimited liability, of secrecy and the impotence of shareholders in plcs, the perverse incentives of share options which led to gross over-remuneration of top management, and to reckless lending by banks, to borrowing by other companies; the facilitatory roles of corporate solicitors and accountants in creating the crisis, all mean that Government must institute an immediate and a radical overhaul of Irish Company law and practice.

The Role of SOEs in Ireland

The areas where the state continues to be involved commercially are as follows:

1. Natural Monopolies
2. Critical Infrastructure
3. Strategic Areas
4. Other Areas of Choice

⁴ This is not aimed at this Review Group but at the Government which instituted this Review. While this Review should be useful, another Review on the Irish private sector’s operations, ethics and company law and practice must soon be instituted by Government.

1 There is no disagreement that the state should maintain a controlling interest in natural monopolies⁵. However, there is an overlap between certain of the companies which are both natural monopolies and which also operate in competitive markets, for example, the ESB and Bord Gas.

The policy in favour of breaking-up such vertically integrated utilities (VIUs) for “competition” reasons, promoted for years by economic conservatives, is no longer in favour in most countries, provided networks are independently regulated. It is widely accepted that there are clear economies of scale and scope for small utilities like Ireland’s. While ESB and BGE may appear to be large in Ireland, they are minnows by world standards and would lose much, with break-up. Congress and many others are of the view that the break-up of VIUs is simply the wrong road especially in a small island economy. For example, the ESB has divested of a substantial proportion of its generating capacity. The commercial and domestic electively supply market have been opened up to competition with the ESB price being set by the regulator and its competitors free to set their prices below that of the ESB. Congress rejects what appears to be an “ideological imperative” to break-up these companies by some.

2 Companies that operate in the area of critical infrastructure include Dublin Port and the Dublin Airport Authority. In ways these are local monopolies too, within defined geographic areas. Thus private local monopolies should be avoided. The definition of what is critical infrastructure is clear-cut, but there are areas where differing viewpoints can emerge on what constitutes strategic infrastructure or corporate entities.

⁵ However, the government did privatise Eircom in 1999, which had a monopoly on fixed phone lines in Ireland. This is unanimously agreed to have been a major policy mistake. It set back the development of the Smart Economy by a decade. The company was profitable, had low debt, was reducing charges and investing heavily while in majority public ownership. After privatisation, it was taken over later by venture capitalists and it ran up huge debts, became highly unprofitable, cut its investment programme dramatically and so eleven years later, its key role in broadband means that nearly all Irish broadband services lag behind most competitor countries. And the state has pumped tens of millions in broadband subsidies, in a vain attempt to catch up, an ambition which is only recently occurring.

3 The third area, that of strategic importance, is one of political choice. The definition of strategic should not be narrowly defined and must encompass national, regional social and other issues, both immediate and in the future. What is strategic may often not be recognised until a crisis occurs. This means that the Review Group must think well beyond the immediate. Thus foresight is a premium.

4 Other areas are useful for jobs or value enhancers or as part of strategic direction chosen by a state⁶. The idea that the state should leave all areas of business is ideological and it is failing. For example, the overnight collapse of the major private banks, Ireland's top companies by market capitalisation, of the huge property developers, of the major builders and many connected firms, demonstrates enterprise failure never seen in the state owned sector. Another example is where the taxpayer sold off the assets Whiddy and the Refinery of the state oil company INPC for €116m (and the state wrote off €78m too) and the private company then sold the refinery alone a few years later for €350m.⁷

Congress recognises the financial crisis and the huge gap between current revenue and expenditure. While many remedies must simultaneously be applied to address the gap, it seems very clear that the sell-off of these companies for short term capital gains (more likely capital losses) to pay current debts would be a policy mistake. Even the capital raised from a large privatisation would be small in bridging the gap and it would be only for one year. Besides, it would be against good prudent accounting / Budgetary practice to utilise capital to bridge a gap in current Exchequer revenue.

To sell SOEs with an major indigenous enterprise deficit in Ireland, and when prices are low is bad politics, bad business and bad economics, but to sell off public monopolies would be a double disaster. This was done less than a decade ago by

⁶ Should we suggest "The Smart Economy"?

⁷ Palcic and Reeves, *Costly Business: Privatisation and Exchequer Revenue* in Progressive Economy, 18th July, 2010.

government which privatised Eircom and its fixed line monopoly, just as we entered what is euphemistically described by the same government as the “Smart Economy.”

As a largely state owned company, Eircom was debt free, profitable and investing heavily in broadband and in its mobile arm. Privatised, it was asset stripped⁸ and is a shadow of its former self. In this so-called “Smart Economy,” we do not have a decent broadband system – thanks to this ideologically motivated privatisation. Many small investors lost much money when they bought shares in their own company. Ironically, it is now owned by a Singaporean state company which seems to be investing in its long term future.

State Owned Enterprises have a Vital Role in the Economy

It has been seen that Ireland has a major private enterprise deficit. We thus need State owned enterprises (SOEs) more than ever. This is not the time to privatise our remaining public enterprises but to expand them within indigenous ownership and control.

Even the OECD has stated that, in spite of extensive privatisation, “state owned enterprises are likely to remain important in many OECD countries.”⁹ While many leading Irish indigenous companies have collapsed, in contrast, all of the remaining state owned companies (SOEs) have performed well during the crisis and indeed have been performing very well for over two decades. As with all firms, most could perform better too.

⁸ See Sweeney Ch 3 on Eircom in *Selling Out* (2004). Valentia Consortium made a gain of €906.5m or a 134% return in just two years on its ownership of Eircom. It paid out huge dividends of over half a billion on *losses*. It paid top four managers €29m in gratitude largely for successfully borrowing €1.1bn which was largely used for payouts to shareholders - not investing in the company.

⁹ OECD, 2005, “OECD Guidelines on Corporate Governance of State Owned Enterprises,”. Paris.
<http://www.oecd.org/dataoecd/46/51/34803211.pdf>

There is a benefit in undertaking this Review which could lead to restructuring and improvements in performance. Further, an innovative approach could point these companies in an expansionary direction, within a new governance structure.

Congress urges that a new governance structure is set up to move shareholder operations away from Government departments to a commercial State Holding Company (the details are set out in the attached document, *A New Governance Structure for State Companies*, 2005). Civil servants do an excellent and complex job, but second guessing commercial investment in companies is not an area where it is fair for them to be working.

Some of the largest indigenous companies are state-owned or are former commercial state owned companies – ESB, BGE, DAA, and privatised, Eircom, Irish Continental Group, Greencore, part state owned Aer Lingus, and the former state banks, ICC, ACC and Irish Life (and Permanent).

The Case Made for Privatisation

Some assert simply that “the state has no business in business.” This is of course not the case in the real world. The state has many roles in business – regulating, making laws, public procurement, etc, but it also has a key role directly in commercial business too, especially in some sectors (see section above).

There were four reasons for privatisations cited by Thatcher in the UK; a) wider share ownership, b) greater competition, c) raising revenue and d) curbing the power of the trade unions. Yet only one of these was achieved – that was wider share ownership and, in time, that ownership was dissipated. The companies were made more competitive while in public ownership prior to sell-off. In general, over the decades the state has loses out in revenue raising or more accurately capital receipts (the great exception was Eircom which was sold at peak price in 1999, before the Dot.com bust). Unions are no less active in the privatised firms and in Ireland were social partners for 22 recent years. If there are issues on efficiency, the initiative should come from management. Since EU rules on competition and the state aid,

many years ago, trade unions, management and local interests (eg sugar plants) and no longer seek subsidies for state (and also private) companies, as was the case for regional and employment reasons for many years. The major and recent exception has been all the privately owned Irish banks.

In Ireland, in Eircom, wider share ownership was certainly achieved with over half a million retail shareholders, but only for a brief period. The fall in price left a very bitter legacy, as did the enforced sale of shares to the private equity consortium.

The Winners and Losers of Privatisation

There are clear winners and losers in privatisation. The Group should consider these and also the potential for unintended outcomes too.

Losers

- Taxpayers - as the companies are usually sold below market value¹⁰ and the state loses dividends, value-adding companies and
- The state which loses strategic companies ie Eircom a fixed line monopoly and the great reduction in its investment for a decade in broadband investment.
- The state also loses top management and head office skills as it is usually moved abroad to the metropolitan state of the new owner.
- Employees, as firms seek to recoup its investment, usually leveraged, by focusing on wages and conditions and redundancies and asset sweating to repay high, leveraged debts.

Winners

- The top management team – excessive and market-distorting share options and inflated pay.
- Underwriters and stockbrokers
- Consultants on both sides – lawyers, auctioneers, accountants etc.

¹⁰ See for example Ch 6 in Sweeney, Paul, 1989, *The Politics of Public Enterprise and Privatisation*. Tomar, Sweeney, in Chapter 6 (sic) in *Selling Out* and “Administration,” Vol 58 no 1, 2010, *Costly Business: Privatisation and Exchequer Finances in Ireland* by Donal Palcic and Eoin Reeves

- Purchasing companies or shareholders, as the shares are usually priced cheap by the underwriters (who would be caught) to ensure they sell.

Thus there is a clear transfer of both wealth and power upwards. As representatives of the 41,000 employees in the commercial state companies, we want to see these companies expand, not shrink.

Ireland and State Companies.

Ireland's state companies have been very successful, and have contributed much to the economic development of the state, the management and worker skill enhancement, to added value, regional development, utilisation of indigenous resources, etc. Yet it is important to review their operations periodically.

Forfas called for a review of these companies to analyse the "rationale for State involvement in specific markets (including determining natural monopolies, capital and other market failures, externalities and equity concerns) in order to determine what the goals of State owned enterprises should be – collectively and individually; and their roles in terms of supporting wider economic growth - through the timely provision of high quality and cost competitive infrastructure. It argued that "privatisation is not an automatic solution to improving the quality of goods and services available to businesses or the performance of state owned enterprises."

The commercial SOEs remain an important part of the Irish economy. However their relative importance was declining, but it has now reversed temporarily and it has increased as the economy has collapsed by a massive 20% in the three years, 2007-2010 and ten or so of the largest Irish private enterprises have also collapsed. The nationalisation of the whole banking sector has seen the size of the state sector expand in a way which no one anticipated, nor wanted. The three largest Irish companies are now state owned enterprises. They collapsed, are pale shadows of their former selves and function only on taxpayers' subsidies. Yet as private companies they were not models of successful enterprise, being essentially corrupt; trading recklessly for several years and were "governed" by boards made up of the great and good of Irish private sector. As employment had collapsed by 263,000

since its peak in 2007, the size of the sector at 41,000 employees, excluding those in the nationalised banks, has expanded marginally.

The SOEs are a mixed group, in many sectors, and include monopolies and companies in very competitive sectors; and in both growing and declining sectors.

Forfas found that:

- “ SOEs’ turnover equated to 5.3 percent of GDP in 2008 and that SOEs employed over 41,000 people directly or two percent of total employment.
- SOEs reported aggregate profits of €426 million after tax in 2008, a fall from €910 million in 2007. SOEs paid share dividends of €170 million to the Department of Finance in 2008 (€484 million in 2007).
- (CIE did receive a subsidy of €321 million in 2008 paid under EU rules for a public transport company). Most SOE revenues come from fees for goods and services provided to their customers.
- SOEs have significant assets and liabilities. The 2008 annual accounts show that the book value of non-current assets is €17.32 billion, equating to 9.5 percent of GDP.
- Clearly, this must be set against net debt of the companies (€3.84 billion) and the large pensions liabilities of some SOEs (€4.31 billion).¹¹

However, these important Irish-owned companies could have been even more successful with a better governance structure. It would be very useful if the issue of governance is addressed by the Review.

A State Holding Company,

The establishment of a State Holding Company, (SHC) is one way of ensuring that a better governance structure for commercial state companies is put in place. Congress believes that it is essential that the companies have a greater commercial focus and one part of this is that it is best achieved with a supportive shareholder.

¹¹ Forfas, 2010, “*Discussion Paper on State Owned Enterprises*”.

The current system of governance is not working well. Thus an expert group of investors within the SHC would make for quicker and more commercial decisions for these companies, in line with policy.

A SHC, as proposed by Congress in 2005, would also free up capital for re-investment in these companies; ensure rapid decisions on major investments; give them clearer objectives; and a developmental role here and internationally.

Forfas also suggested “establishing a single, competently resourced agency dedicated to SOE supervision which could improve the State’s ability to exercise ownership efficiently and monitor companies under its ownership” though it also proposed an alternative of separating the policy and shareholder functions “to ensure greater transparency and more conscious decision making where conflicts between goals exist” and paying for non-economic services which are imposed by the state on these companies.

Further, the SHC can and should be used to leverage their considerable assets for borrowing, outside the strictures of the EU’s Growth and Stability Pact, which can also be used for a major Investment Stimulus Programme for jobs. Congress now knows that this is definitely feasible, but it is not to be considered by the Review Group as determined in its terms by a government determined to cut and cut.

Developing Indigenous Companies

It was seen that some of the largest indigenous companies are state owned or former commercial state owned. It was also seen that the performance of many, though not all, leading Irish private sector indigenous firms has been very poor. These enterprise failures have been very costly to many workers and not alone did some of the leading companies collapse, but their appalling management nearly bankrupt the Irish state.

With some leading Irish indigenous private companies so badly managed over recent years, innovative thinking on the development of our better companies is urgently

required and state-owned or partly state-owned companies, mutuals and coops must play roles in such thinking. The private “shareholder value” model of company governance or even a modified version of it, is hardly the only corporate structure of enterprise after recent events.

Corporate Governance of private companies has to be radically reformed moving sharply away from “shareholder value” to a wider stakeholder model. This has to be done by radically reforming Irish company law. It is not sufficient to solely review the governance of the commercial state-owned companies without having a parallel group to this Review to also simultaneously reform Irish company law for all companies.

A State Bank

Ireland had two development banks ICC and ACC for many years and they both served the SME and farming sectors well. They were sold off in the era when privatisation was in fashion in the 1990s.

Had the state banks not been privatised in 2001, less than a decade ago, maybe all Irish banks would not have collapsed. State banks should have had longer term perspectives, than the private banks, as they would not have had the perverse incentives engineered by their greedy managements, hand in hand with their boards and thus should not have engaged in grossly irresponsible lending. The sale of the state banks was a major policy mistake. RBS bought ICC ten years ago. It is withdrawing from Ireland, leaving the employees without jobs when the SME sector is crying out for credit.

It is said that over time, the profits made by the world’s banks is equal to zero, thanks to massive bank collapses. We propose that the Review must recommend that at least one bank is retained in public ownership to ensure credit is never stopped again for business, as happened with Ireland’s banking sector.

The Internationalisation of SOEs

Many of the Fortune list of the top companies are former state-owned companies in many Western countries and many are still state owned. In short, state companies have played a major role in developing some of the biggest enterprises of global scale throughout the world and continue to do so. The role of state owned enterprises is important from a policy perspective. Thus this Review of the Irish state owned companies must think in terms of developmental strategy, in short-term cash raising.

The Review Group should consider promoting an active role for increasing the internationalisation of Ireland's state-owned companies. It should seek to assist in clarifying the Irish government's policy in terms of the international activities of SOEs. To date there have been start/stop policies eg in regard to the expansion of ESB and DAA in the past. Nonetheless, they are important in Ireland's overseas foreign investment, which is a vital part of a small open economy. Selling them off or their international branches would diminish Ireland's commercial global reach.

Had there been an more active developmental policy towards these state companies over the past 25 years, instead of a what at times, was a restrictive and hostile one by Government, they could have become world leaders. The ESB has a major power plant in Spain and several in the UK. It was prevented from making a major investment in Poland, one of only two OECD countries not to have had a recession, after the 2008 Crash, by the government for reasons not explained.

The DAA (as Aer Rianta) was a major airport operator and was investing in buying and operating airports internationally, until it was curbed by the Department of Transport. It also sought to invest in Dublin long before the new terminal was required, but a report by "independent consultants" hired by the Department of Transport, led to the company being ordered "to sweat its assets," to our cost. It had bought Birmingham and Dusseldorf airports in partnership with private firms, but it was the operator of both. It would have bought and operated many more airports had it not been stymied by the unsupportive shareholders in Government, specifically in the departments of Finance and Transport.

Some policy makers believe that Ireland's reliance on Foreign Direct Investment (FDI) is under threat as FDI begins to move to emerging economies, especially in Asia. If this is correct, and we must be vigilant as we will increasingly have to rely on indigenous enterprise for job and wealth creation. Ireland has some very fine Irish companies. But we have also seen that whatever the deficiencies of some state owned companies in the past, they pale, utterly, when compared to the incompetence of many, though not all, of the Irish indigenous corporate elite in the private sector on the banks board and related companies¹². Thus new forms of enterprise are needed, including state owned, public-private partnerships, mutuals and cooperatives, (as in the food sector) etc.

Other countries are utilising their state companies and Sovereign Wealth Funds (SWF) to invest strategically in their own interests. Those that are still selling off are countries still with very large state-owned operations, which have been used as arms of the state rather than commercial enterprises.

The Norwegian State fund became one of the largest shareholders (6.5%) in Smurfit Kappa, one of Ireland's leading indigenous multinationals this year. CNOC, the Chinese state oil company is a partner with Irish company's Tullow Oil's find in Africa. The CIC is a massive Sovereign Wealth Fund owned by the Chinese government which is buying up shares in companies all over the world.

Chinese companies, private investors, sovereign wealth funds and state-owned companies are investing heavily in many parts of the world. The Chinese state recently became one of the biggest shareholders in Guinness' parent, and Volvo car was bought by an obscure Chinese carmaker, Geely. Chinese strategic investment internationally is massive, quite strategic and mercantilist.

Thus, there are major economic trends occurring which do not conform to liberal economic theory. Chinese state companies are taking shares, in varying amounts, in

¹² Too see the links of interconnected banks directors with other leading firms in the private AND public sector, see *Mapping the Golden Circle*, TASC, 2010.

all kinds of companies worldwide, through stock markets, trade sales etc. While Congress has issues with many aspects of the operations of Chinese companies, on civil and worker rights, it is important to note international developments by these and other companies.

Back in 2007, the Chinese Investment Company (CIC) purchased \$5.6 billion in MS common stock, or 9.86% equity ownership in Morgan Stanley and in the Blackstone Group, a major private equity fund. It and other state companies are investing in many companies worldwide for strategic reasons eg coal in Canada, oil in Russia, steel in Brazil and in farms and natural resources in much of Africa etc. Chinese companies, like CIC, Sinopec and CNPC, spent \$24.6bn buying oil and gas companies in the first ten months of 2010 alone.¹³

The Future of SOEs

There are new areas where the state might intervene directly in the economy in emerging Infrastructure and other enterprise related area like bandwidth and emission trading – areas which are relatively new and where the state can play a very important development role. In some cases, the state itself, through corporatised entities may be the best player from a national perspective. Or it could co-operate with private firms in joint operations too. In others, auctioning and licensing may be the best path.

It is argued that SOEs should not enjoy a competitive advantage simply because of their State ownership. This was the case in the past but they no longer have that advantage, under EU rules on state aid. However, there are state firms in key areas for legacy reasons and provided they deliver on services, they should retain their position. It is not sufficient to impose radical change which undermines workers' jobs, their job security and conditions, simply as an experiment with an economic model which has failed in so many ways within the past five years. The saving made from extracting savings from labour is eaten up in profits and reductions in services, as has been demonstrated through privatisation in many areas.

¹³ Financial Times, 8th Nov 2010.

Conclusion

Congress regards this Review as extremely useful, provided the Group takes a wide interpretation of its restrictive terms of reference. It should take a strategic view, and examine the case for reorganisation, for development and growth of SOEs. It should also resist the pressure to make the case for fire sales. The Group should also consider that by the time its work is completed, its report may well be in the hands of a government which may take a longer term view of these SOE companies, than as “cash cows” to be sold off to pay pressing day-to-day bills.

Privatisation would reduce the number of key indigenous Irish enterprises substantially. It would reduce annual cash flows to the state in dividends and the productive asset base of the state. It would therefore be counterproductive to sell off some of the best and largest Irish companies, most likely to foreign multinationals, (for the reasons given above).

The Review Group could recommend the sell-off of these productive SOEs for cash. It would then be recommending a course of action which is contrary to good business practice - where capital assets are sold to pay day to day bills. To sell monopolies would be worse. To sell when prices are as low as they are today would be bad business. If there is to be any change in Ireland’s Balance Sheet from privatisation, it will *reduce* it, as privatisation sell-offs are pitched low to sell, even in good times and transaction costs to the many professional middlemen are high.

To recommend the break up of Vertically integrated utilities simply to sell off the competitive bits, where Irish VIUs are minnows by international standards, would lose the economies of scale and scope of these enterprises. This is particularly true when there is no need for such action, except perhaps an adherence to a particular ideological economic outlook.

The interaction of the State and Enterprise is complex, as we have learnt to our cost. Now the top Irish private firms – namely the banks - failed and are costing taxpayers

a great fortune. We have an enterprise deficit which the SOEs can help address with the assistance of this Review. This Review should really be paralleled by another Review on Governance and Competence in the private sector.

With some vision and innovative thinking, the Review could see these Irish SOEs as vehicles to be harnessed, together with the private sector in cases, to develop the Irish economy.

There is a New Enterprise Paradigm as leading Irish private companies have collapsed, with huge losses which have endangered the state itself. The taxpayer has bailed many of them out, and the full costs are yet unknown. Further, more Foreign Direct Investment may shift, over time, to emerging economies. It has played a vital role in Ireland's economy and will continue to do so, but we have to prepare for a possible decline over time and State-owned companies, which are performing well and are still among the largest Irish indigenous companies, have a role to play in the new enterprise paradigm.

Instead of a relatively passive, small-scale approach, as has been the Government policy on state companies up to now, we could be bold and innovative. If the scale of FDI does reduce, and with the enterprise deficit left by the legacy of so many "leading" Irish private sector companies, we really do not have a choice but to take the "high road" – the developmental road - with our state companies as key players.

As Forfas concluded "It is difficult to discern a definitive national policy on SOEs in Ireland - the practice to date has been to approach issues on a case by case basis rather than an overall strategic approach." This Review can help on this policy area.

There is also a need to evaluate the goals of State Owned Enterprises in Ireland's longer term strategic interests. For example, Congress has long argued that energy security will soon be extremely important and SOEs should have a vital role in the area, in addition to government departments, as players in the energy markets. Water and waste is an important public area which could benefit from a new SOE

utilising NPRF capital and existing public assets, with minority private investment in a joint venture, to commercially expand and improve delivery.

Over time, the profits made by the world's banks is equal to zero, thanks to massive bank collapses. Congress urges that at least one bank is retained in public ownership to ensure credit is never stopped again for business, as happened with Ireland's banking sector.

The Group must recommend improvement in governance to release the commercial potential of these companies, through a State Holding Company. The Review could add real value by also recommending that the state utilise the enterprise potential of these key indigenous SOE companies to develop in Ireland and abroad, utilising the cash available within a SHC structure, as suggested by Congress in 2005.

It is important not to sell off productive enterprises/assets rather than develop them to create more value and jobs. It would take a long time to build up an enterprise like the ESB or RTE. Even with a huge fiscal deficit and a rising net national debt, the real question is - can we afford to sell these iconic enterprises to EDF, Eon or British Airways or Blackstone Group?

Some years ago the state appeared to be withdrawing from the economy.... but it was simultaneously expanding into new areas like regulation and was establishing new operations and spheres of influence. The state grows and retreats over time from different areas of the economy, but it is back in a major way bailing out the private banking sector and it is also directly involved in business. The challenge is not to remove the state out of its many roles in enterprise, in business, but to ensure its role is effective and that its direct involvement in enterprise is value and job enhancing.