

Sweden: bold, novel approach

The first attempt by a European government to address systematically the ownership and management of government enterprises has rapidly yielded significant returns and benefits. By **James Sassoon** and **Martin Pellbäck**, UBS Warburg.

Three cases illustrate the Swedish Government's bold and novel approach, which is likely to be followed by many others as the pressures on efficiency, prudence and transparency in the government sector increase:

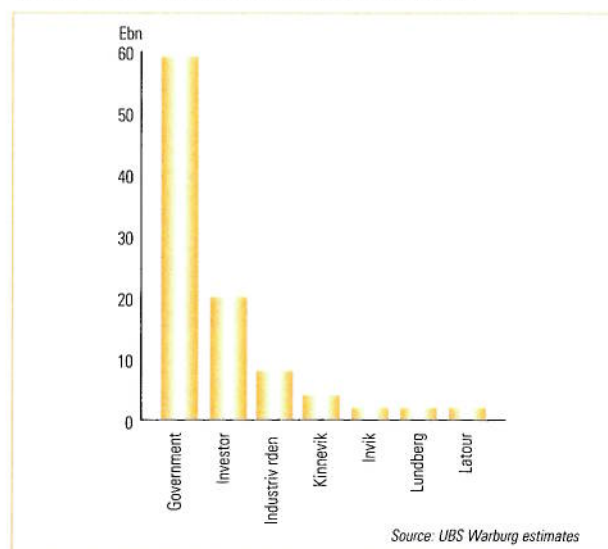
- the restructuring of AssiDomän, one of Europe's largest paper and packaging groups and a significant owner of forestry assets, by divesting or joint-venturing parts of the industrial operations and returning capital to shareholders;
- the restructuring and subsequent sale of Celsius, one of Europe's largest defence groups, which involved finding suitable industrial partners for several of Celsius' business areas; and
- the transformation of SJ into one of the most profitable rail operators in Europe, by streamlining and divesting all operations other than its core passenger traffic services.

What these three cases have in common is not only that they involve large Swedish companies undertaking major transformations to improve performance and create shareholder value, but also the key role played by the Swedish Government in accordance with its new ownership policy. Considerable progress has been made, thanks to the pragmatic and commercial approach taken, and despite the inherent complexities of operating in a political environment in general and in a minority government in particular. In this article we summarise the key points of the Swedish Government's ownership policy and how the programme is progressing two years since its inception.

Significant Government ownership

The Swedish Government is the country's largest owner of enterprises, both in terms of value and number of employees. The value of the Government's portfolio is estimated at E60bn (US\$51bn at the exchange rate of 14 November 2000) and there are indications that the companies represent approximately 25% of the domestic Swedish business sector. The portfolio includes some of Sweden's largest companies and the

Graph 1: estimated value of portfolio (Ebn)



combined headcount is over 200,000 employees. The 63 Government-owned companies include a wide variety of businesses in terms of size and operations, ranging from the telecommunications operator Telia to the Royal Opera and businesses with revenues of only a few million. Certain businesses retain monopoly positions, but more than 80% of the companies operate in competitive markets.

Graph 1 illustrates the estimated value of the Government's holdings compared to the assets of the largest Swedish private sector investment companies.

Table 1 shows how the ten largest Government-owned companies rank by sales compared to other Swedish companies.

Active ownership policy

The Swedish Government does not have a policy to privatise Government-owned companies. Decisions on privatisation are taken on a case by case basis when this is deemed to be in the best interest of taxpayers and the relevant company. The Government has, however, ruled out privatisation of natural monopolies.

Given the size of the Government-owned company sector and the absence of a policy to privatise, the Swedish Government has developed an ambitious programme for managing the companies as an active and professional owner. The policy includes setting clear objectives and guidelines for the development of each company and measuring performance against these targets. The overall goal is to create shareholder value and, where relevant, to serve specific societal interests in an economically efficient manner. The Government's vision is that the companies shall become the most well managed and well-reputed companies in their respective industries.

Photo: Imagebank, Nybroplan, Stockholm, Sweden



A specific ownership function has been established within the Government administration for the development of the ownership programme and the management of the portfolio. The ownership function is separated from regulatory policy decisions and, subject to special objectives where relevant, the remit is to act like professional value-maximising investors. Staffing has been bolstered by finance and management professionals recruited from the private sector.

The three principal tools for implementing the ownership policy consist of transparency, capital structure and board nominations.

Transparency comprises agreeing on clear objectives and targets, creating a high quality reporting structure and encouraging interest and openness regarding performance. The external reporting of the companies shall be comparable to that of publicly listed companies, both in terms of content, speed and frequency of reporting. The purpose is to increase transparency and facilitate benchmarking with relevant competitors in the private sector. The companies are encouraged to open their annual shareholders' meetings to participation from politicians, the media and members of the general public. Independent analysts have evaluated several companies and seminars have been organised where companies present themselves and financial analysts are invited to challenge the management teams on strategy, performance etc.

Table 1: Government-owned companies ranked by sales

Company	Sector	1999 sales Ebn	Ranking by sales
Telia	Telecoms	6.1	15
SAS	Airlines	4.9	17
Vattenfall	Utilities	3.4	26
Nordea	Financial services	3.2	28
Apoteket	Retailing	3.1	29
AssiDomän	Paper & packaging	2.9	31
Posten	Postal services	2.8	32
Systembolaget	Retailing	2.0	45
SJ	Rail transport	1.8	48
Svenska Spel	Gaming	1.6	56

Source: Veckans Affärer

Capital structure analysis is the main tool for allocating capital between companies and creating value through optimising individual companies' capital structures. In certain instances, analyses have shown that companies are over-capitalised and that significant amounts of capital can be returned to shareholders. As a complement to the analysis of capital structure, several companies have adopted value based management systems, in some instances coupled with incentive schemes for the employees.

Board nomination is the principal tool for improving the execution of companies' strategies. Nominations to the boards of directors of the companies shall be transparent and shall aim to secure the key competencies required by each company. A process of evaluation and nomination is undertaken each year by the ownership function in co-operation with the chairman and chief executive of each company. The aim is to attract more private sector experience to the boards, where relevant.

The Government has developed and published detailed guidelines on a number of these topics. In addition to improvements in the external reporting of the companies, the Government has improved its own external reporting. The annual review has been expanded and improved and the publication of quarterly reports has been initiated in 2000. These documents, along with comprehensive materials on the Government's ownership policy and information on the Government-owned companies, are also available on the Government's website, www.industry.ministry.se.

Another key initiative that is being actively pursued by the ownership function is encouraging "e-transformation" within the companies, to capture cost reductions and improve the ability to offer customers new services. Significant efforts are being made to develop further the companies' use of information technology in areas such as sales, customer service, procurement and logistics, as well as in enabling new business models. A recent survey commissioned by the Ministry of Industry showed that 60% of the large companies have such projects under way, with the remainder planning to start major initiatives in 2001.

High transaction activity

The Government's policy is for the companies to grow their core businesses and to streamline operations by divesting unrelated businesses. The level of transaction activity has been high and in addition to transactions undertaken by the portfolio companies, a number of divestitures have been made at the Government holding level. The most significant transactions relating to Government-owned companies in 1999 and 2000 until the end of October include:

Acquisitions by portfolio companies

- acquisitions by Vattenfall, the wholly owned electricity company, of electricity companies and participations in Finland, Norway, Germany, Poland and the Czech Republic;

- acquisitions by Vin&Sprit, the wholly owned spirits group, of spirits companies in Denmark, the Czech Republic and the UK;
- acquisitions by Nordea (formerly MeritaNordbanken), the 18% owned financial services group, of UniDanmark in Denmark in March 2000 and of Christiania Bank og Kreditkasse in Norway in October 2000;
- the acquisition by Telia in June 2000 of Netcom ASA, Norway's second largest mobile telecommunications operator.

Divestitures and restructurings by portfolio companies

- the restructuring in June 1999 of the paper and packaging group AssiDomän, whereby the Government reduced its ownership from 50% to 35% in exchange for a 100% shareholding in Sveaskog, a company that took over approximately one third of AssiDomän's forestry assets;
- the sale, announced in June 2000, by Sweden Post of Postgirot Bank to a group of Swedish banks;
- the sale by AssiDomän in August 2000 of certain paper and packaging operations to Frantschach of Austria;
- the announcement in October 2000 of the creation of Billerud, a packaging paper joint venture between AssiDomän and StoraEnso.

Divestitures at the Government holding level

- the sale in January 1999 of the Government's remaining 7% in the pharmaceuticals group Pharmacia&Upjohn in a E1.8bn share offering;
- the sale in July 1999 of the Government's 50% holding in the Swedish central securities depository VPC to a group of Swedish banks for E70m;
- the sale in February 2000 of the Government's 25% shareholding in the defence group Celsius for E150m, in connection with a public offer by Saab for Celsius;
- the E8.8bn initial public offering in June 2000 of the telecommunications group Telia. The offering raised E7.4bn for the Government and E1.4bn for the company. The Government's holding following the IPO amounts to 70.6%.

Despite the absence of a policy to privatise, the Swedish Government's pragmatic approach has resulted in significant disposals, with sales at the Government holding level raising proceeds of approximately E11bn in 1999 and 2000.

The Government has been authorised by Parliament to sell its remaining 18% shareholding in Nordea. The Government has stated its intention to do so, but not the timing of the sale. Further privatisations will, in accordance with the Government's policy, depend on the development and specific circumstances of each portfolio company. However, a continued focus on core activities is likely to result in further divestments from some of the Government-owned companies, such as Telia, SJ, Vattenfall and AssiDomän.

Progress of the active ownership policy

The Swedish Government's ownership policy has many positive aspects. The Swedish Government is the first European government systematically to address the issue of managing Government owned companies. The size and diversity of the Government holdings means that the programme is being followed closely by other countries.

It is a programme, which, if well executed, will maximise value through higher annual returns or through higher prices if and when assets are sold.

Improvements in the performance and value creation of the Government-owned companies will benefit the Swedish economy as a whole, given the size of the Government-owned sector.

Improvements in reporting and communication have created greater transparency, a vital ingredient in focusing the attention of politicians and taxpayers on the performance of their portfolio.

It is notable that the Government's ownership policy has broadly been supported by the trade unions within the Government owned-companies, where the Government's motto "valuable companies create valuable jobs" seems to have struck a chord.

However, questions are being asked about the merits of active ownership relative to privatisation. Recent Swedish economic research shows a clear negative correlation between the size of the public sector and growth in the economy.

There also remain certain areas where further progress can be made, including:

- the determination of financial, strategic and operating targets for the portfolio companies remains to be completed as well as systematic procedures for evaluating and communicating performance against these targets;
- the process of separating public administration functions from commercial activities has not been completed in all instances and several entities within public administration bodies are in the process of being incorporated;
- changes in the capital structure of companies have not yet been fully implemented. Part of the difficulty in the implementation is no doubt linked to the lack of flexibility regarding capital increases, which currently require parliamentary approvals;
- board appointments do not yet make full use of private sector expertise and appointments are not yet entirely free from political motives.

The ownership policy of the Swedish Government is an innovative and ambitious new approach to public sector ownership and important progress has been made. The programme has received considerable attention from other governments and from the media and other commentators in Sweden and internationally. One example of this is that the Swedish Government was invited as the main speaker at an OECD seminar on Government ownership and corporate governance in September 2000. ♦