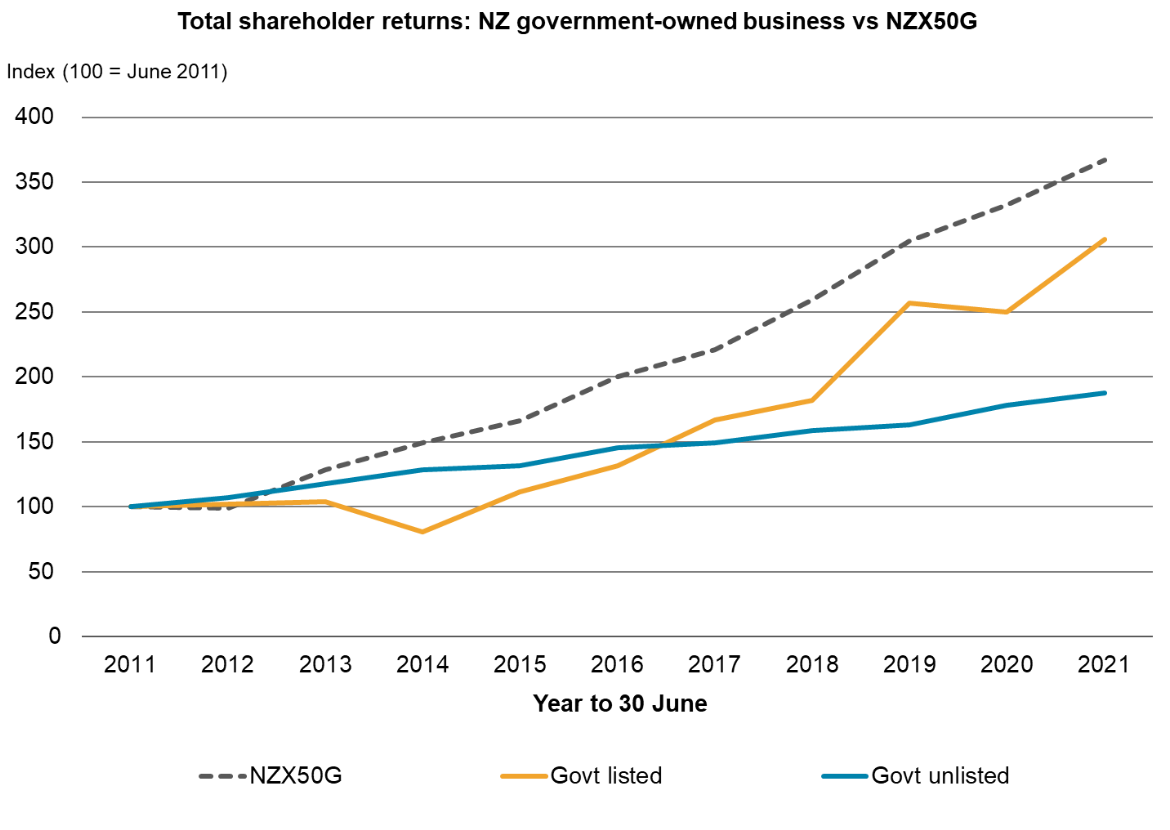
How are the Government’s Commercial Businesses Faring?

Philip Barry

Like many countries, New Zealand has a long and sad history of the government owning commercial businesses. The reforms from the State-Owned Enterprise Act passed back in the late 1980s saw some impressive gains in performance but the Treasury’s latest Investment Statement suggests those improvements are not being sustained.

Currently, the government owns or part-owns eighteen large commercial businesses with combined assets totalling $78 billion. These businesses include three electricity generator/retailers, an airline, a post/courier company, a bank and minority stakes in three airports amongst other enterprises. Together these commercial enterprises account for 10% of the government’s net worth.

The Treasury finds the financial performance of the 100%-owned government businesses has been particularly unsatisfactory. Fourteen of the eighteen companies are 100% central or local government-owned. These companies have achieved an average total return to shareholders of 6% p.a. over the last ten years, well below the return achieved by their private sector counterparts (see the graph below). The total returns of the top 50 listed companies (NZX50) have averaged 14% p.a. over the same period.



Source: NZ Treasury

The government entities that are partially privately owned – the three electricity generator/retailers and Air NZ - have done better overall. The total shareholder return of these “Mixed Ownership” companies has averaged 12% p.a. over the last ten years, much better than the 100% government-owned companies but still below the 100% privately-owned companies on the NZX50. The government’s investments in the three energy companies have fared very well but Air New Zealand has been heavily impacted by COVID-19 and has recently announced a $2.1bn recapitalisation plan.

The table below ranks all 18 government-owned businesses in terms of their return to the government as shareholder over the last ten years. As the table shows, the best performer has been the smallest enterprise, Animal Control Products with an average return of almost 24% p.a., followed by AsureQuality and Mercury with average returns of around 15% p.a. The poorest performers have been state-owned broadcaster TVNZ and the state-owned farmer, Landcorp, both of which have provided little or no financial return on the government's multi-million dollar investments over the period.

Total Shareholder Returns on Government-Owned Businesses, 2011 to 2021, % p.a.

	% p.a 2011-21	Commercial Valuation NZDM, 2021
Animal Control Products	23.7%	11
AsureQuality	15.6%	241
Mercury	15.0%	4,777
Dunedin Airport	14.9%	46
Transpower	12.4%	1,811
Meridian	12.3%	6,969
QV	10.1%	24
Hawke's Bay Airport	9.8%	17
Genesis	9.7%	1,818
Air New Zealand	9.7%	903
Christchurch Airport	9.1%	343
Public Trust	8.7%	83
Airways	8.5%	272
New Zealand Post	5.8%	1,706
Kordia	4.0%	139
MetService	3.0%	59
Landcorp	0.4%	1,380
TVNZ	0.0%	237

Source: NZ Treasury

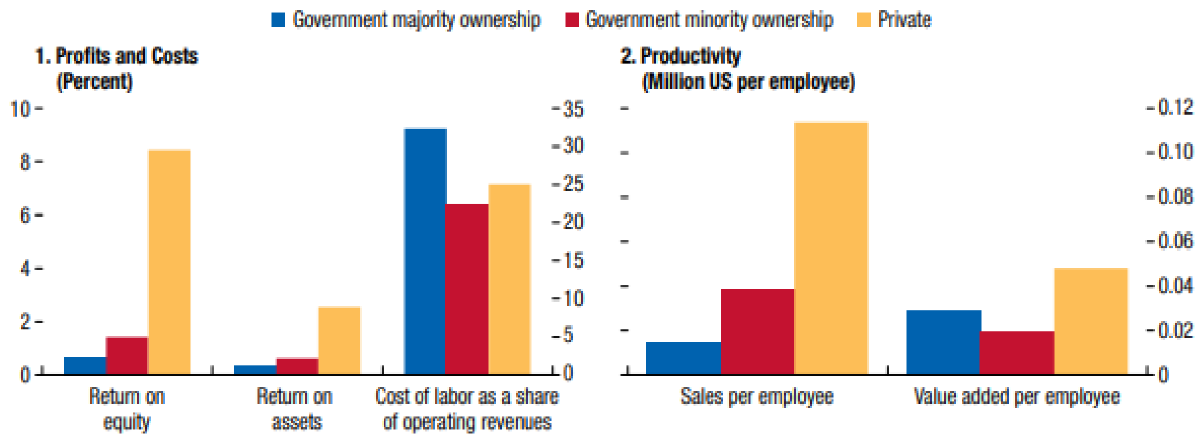
The poor performance of the 100% government-owned business is evident not only in their returns to shareholders. Their revenue, earnings and dividends have all trended down over the past five years.

NZ's experience with 100% government-owned and partially privatised companies is fully consistent with the experience from other countries. The graph below summarises the IMF's findings on the relative performance of businesses that are government-majority owned, government minority-owned and 100% privately owned. The findings are based on a sample of almost 1 million companies across 109 countries.

As is the case in New Zealand, the IMF finds that enterprises with a majority government ownership have the lowest return on equity, the lowest return on assets and the highest costs. The majority government-owned enterprises also have the lowest productivity – private firms are three times more productive.

As is also the case in New Zealand, the IMF found that enterprises with a minority government ownership performed better than those with a majority government ownership, but not as well as the 100% privately-owned firms.

International Evidence on SOEs' Performance Relative to Private Firms



Source: IMF Fiscal Monitor, April 2020.

These findings from NZ and other countries on the relative performance of government-owned businesses matter. Compared with other similar countries, government-owned businesses play a relatively large role in the New Zealand economy, with assets equal to around 35% of GDP. This compares with the average for the OECD of around 29% of GDP. According to an OECD assessment, the scope of SOEs in NZ is 50% greater than in Australia (federal and state combined).

Some proponents of state ownership of business argue that SOEs have broader public-policy objectives that go beyond financial returns. But the questions are how transparent are those other objectives and are the objectives being achieved in the least costly way. By accepting inferior returns from its government-owned businesses the government may in fact be undermining its ability to achieve many of its broader public policy objectives. If the 100% government-owned businesses were achieving returns comparable with the NZX50 companies, the government would be receiving hundreds of millions of dollars more every year in shareholder returns that it could put toward its health, education, defence or other objectives.

Investment in commercial business is a risky activity that governments are rarely well-placed to assess and manage. The government has been required to inject capital into five of its eighteen commercial businesses in recent years, at a total commitment of over $2 billion. The great bulk of that went to Air NZ, but Airways, NZ Post and Hawke's Bay Airport also received funds.

New Zealand has a well-known productivity problem. It also has a growing public debt problem, with the government's net debt projected to reach 40% of GDP next year. Reducing its stake in commercial enterprises seems an obvious option for the government, regardless of its political colour. It would permit the government to pay down debt, strengthen its balance sheet and prepare for the next economic crisis, whatever its nature. It would also bolster the productivity of the companies and the economy as a whole. A more resilient and a more productive economy is likely to good for the nation's wellbeing.

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