

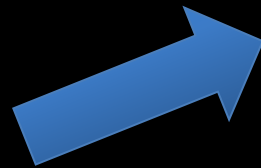
TRENDS IN STATE CAPITALISM AND SHORT TERM GLOBAL RISKS

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Harvard Business School,
Brandeis University and
NBER

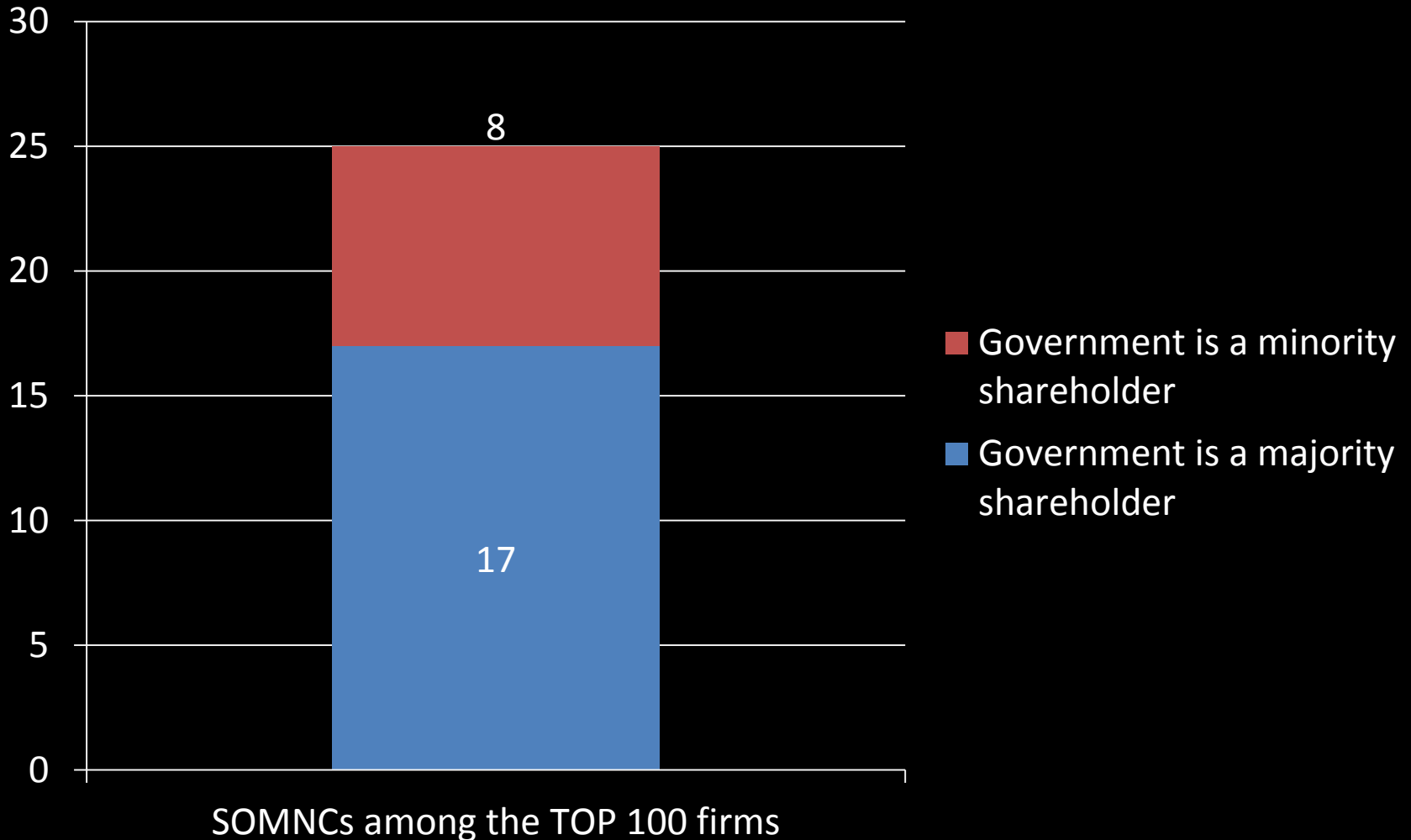
- Top firms in Fortune Global 500 in 2012

What do the firms in yellow have in common?

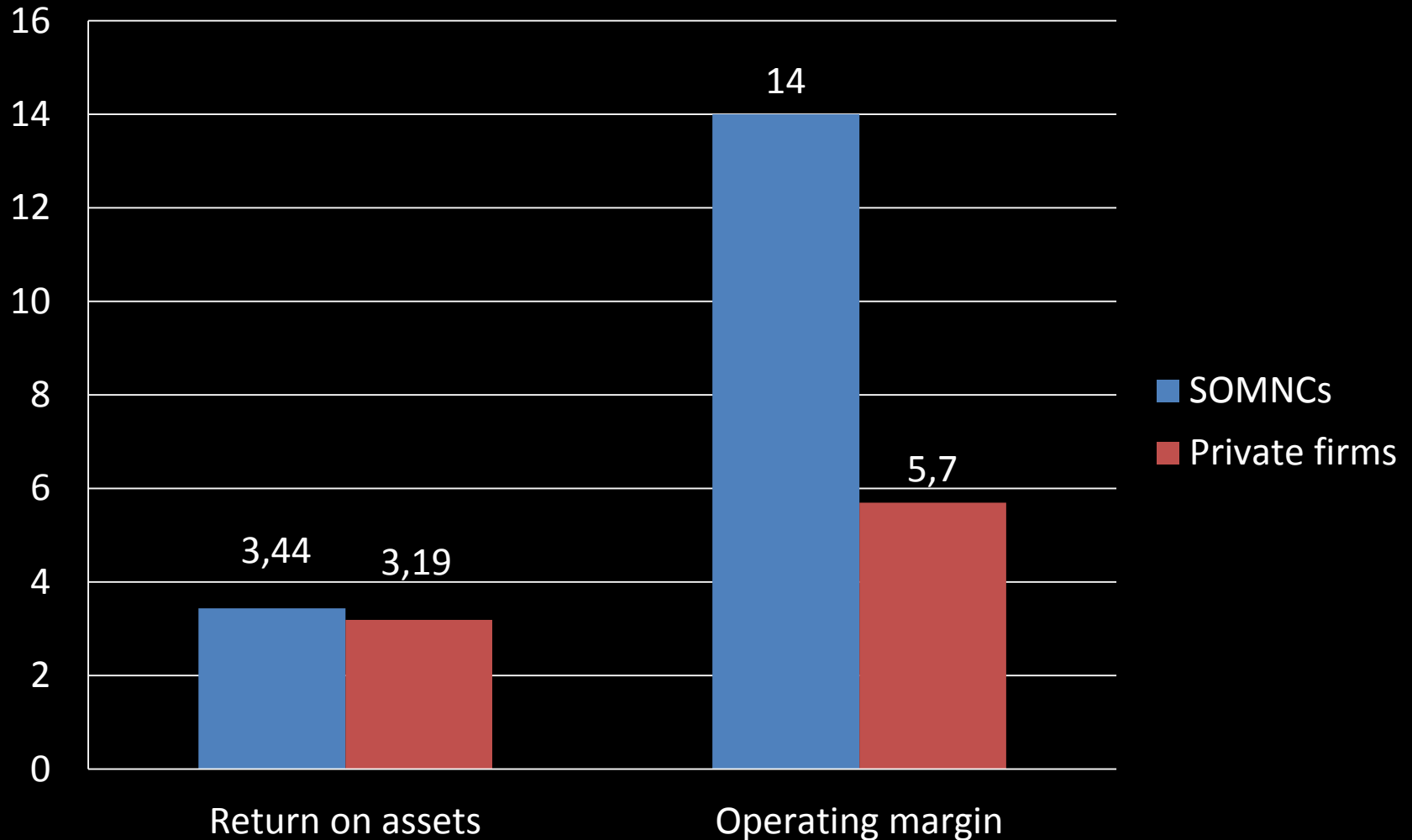


Rank	Company	Revenues in US\$ millions
1	Royal Dutch Shell	484,489
2	Exxon Mobil	452,926
3	Wal-Mart Stores	44,695
4	BP	386,463
5	Sinopec Group	375,214
6	China National Petroleum	352,338
7	State Grid	259,142
8	Chevron	245,621
9	ConocoPhillips	237,272
10	Toyota Motor	235,364
11	Total	23,158
12	Volkswagen	221,551
13	Japan Post Holdings	211,019
14	Glencore International	186,152
15	Gazprom	157,831
16	E.ON	157,057
17	ENI	153,676
18	ING Group	150,571
19	General Motors	150,276
20	Samsung Electronics	148,944
21	Daimler	148,139
22	General Electric	147,616
23	Petrobras	145,915
24	Berkshire Hathaway	143,688
25	AXA	142,712
26	Fannie Mae	137,451
27	Ford Motor	136,264
28	Allianz	134,168
29	Nippon Telegraph & Telephone	133,077
30	BNP Paribas	12,746
31	Hewlett-Packard	127,245
32	AT&T	126,723
33	GDF Suez	126,077
34	Pemex	125,344

25 OUT OF THE LARGEST 100 FIRMS IN THE FORTUNE GLOBAL 500 ARE STATE-OWNED MULTINATIONALS (SOMNCs)



Profitability of state-owned multinationals vs. private firms among the TOP 100 *FORTUNE* GLOBAL FIRMS, 2012



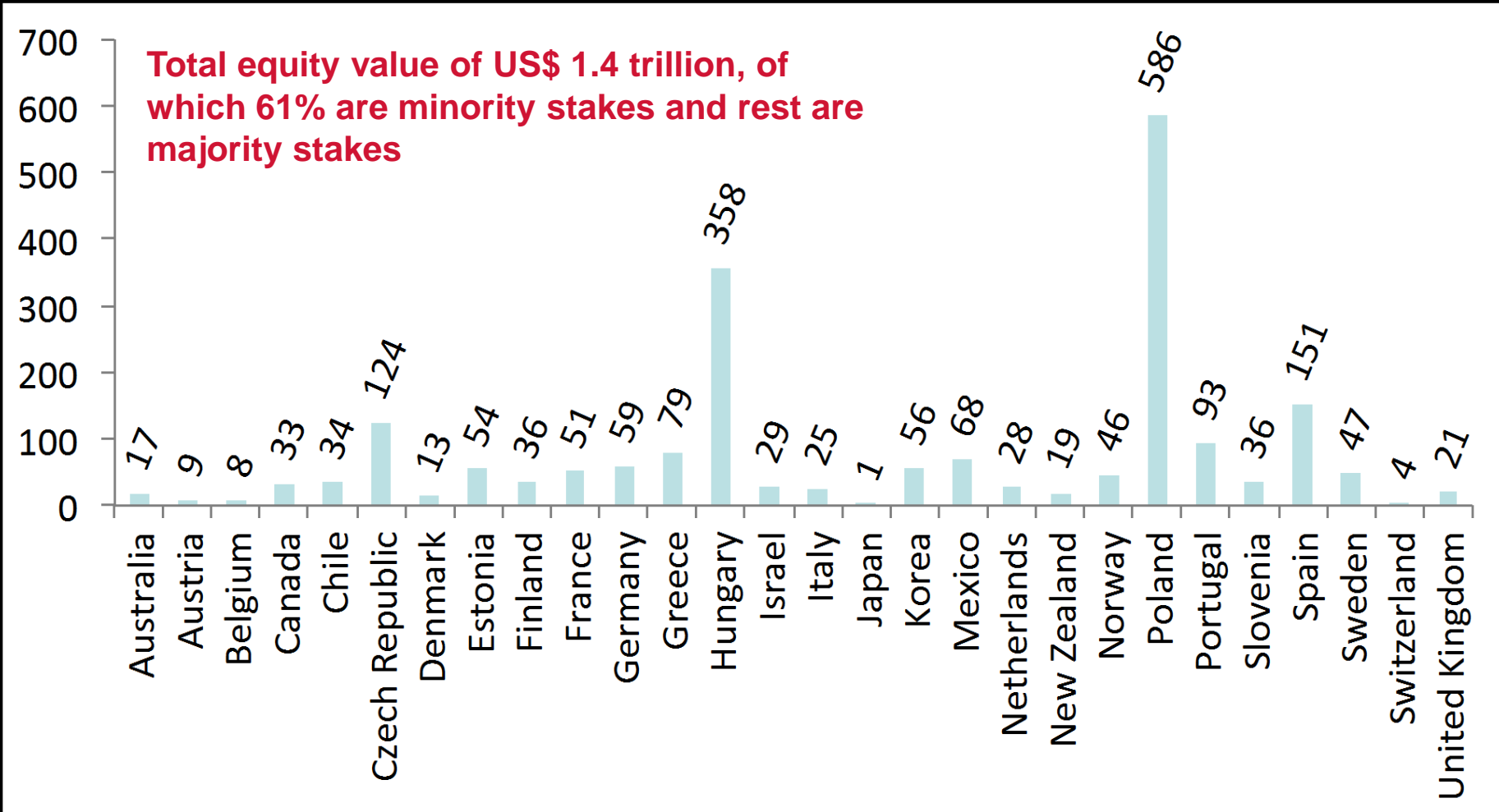
ALDO MUSACCHIO SERGIO LAZZARINI

REINVENTING STATE CAPITALISM

LEVIATHAN IN BUSINESS,
BRAZIL AND BEYOND



The REINVENTION of state capitalism means governments are still owners of a large number of SOEs (FIRMS with gov't as majority owner—OECD)



Resilience of SOEs in EM

	Number of SOEs with majority control		Num. of firms in which the federal government has minority ownership
	Federal	State/local	
Brazil	247		397
China	17,000	150,000	
Egypt	57		59
India	217	837	404
Indonesia	142		21
Malaysia	52		28
Mexico	205		
Poland	498		691
Russia	7,964	250	1,418
Singapore	20		
South Africa	270		
Thailand	60		
Turkey	74	700	67
Vietnam	1,805	1,559	1,740

NEW VARIETIES OF STATE CAPITALISM (Musacchio and Lazzarini, 2014)



Leviathan as an entrepreneur (owner/manager)

- Full state control and ownership of SOEs, with limited autonomy and transparency

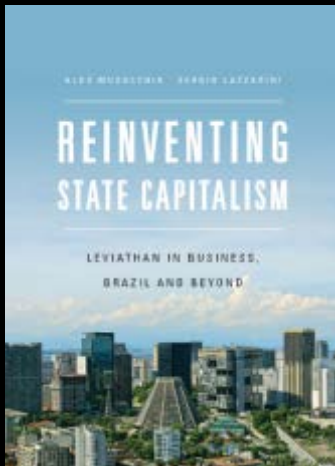
Leviathan as a *majority* investor

- Publicly traded SOEs with improved autonomy and transparency
- State-owned holding companies (SOHCs)

Leviathan as a *minority* investor

- Partially privatized firms (PPFs)
- Minority stakes under state-owned holding companies (SOHCs)
- Loans and equity from state-owned and development banks
- Sovereign wealth funds
- Other state-controlled funds (e.g. pension funds, life insurance companies).

Privately-owned firms

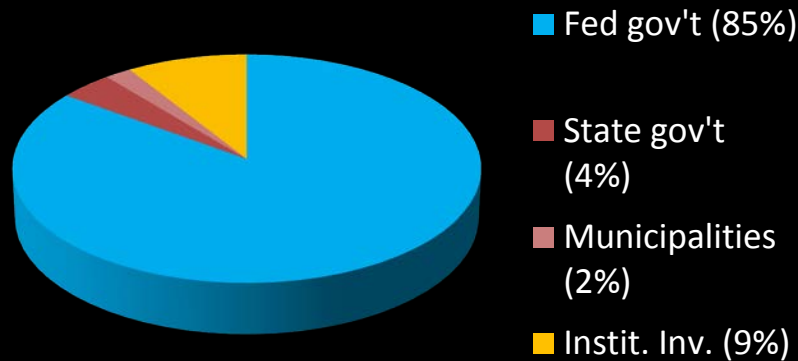


LEVIATHAN AS A MAJORITY INVESTOR

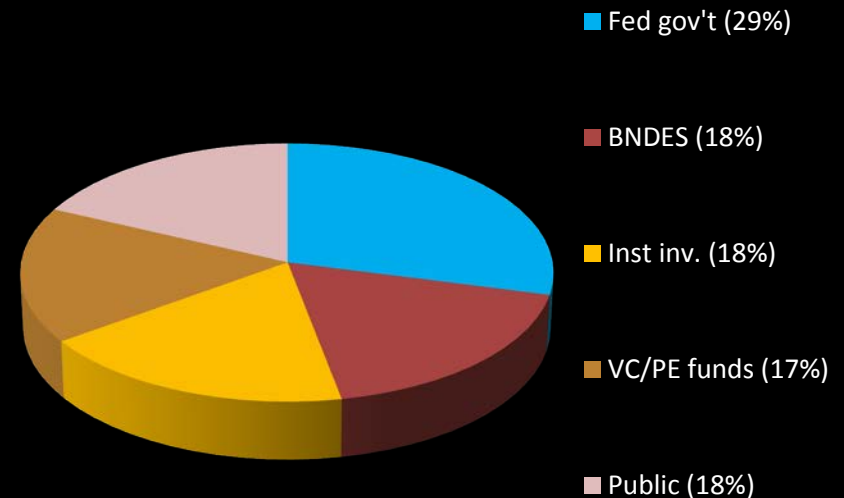
- Large state-owned enterprises are **listed in stock exchanges**.
- They bring in **active investors as monitors** (pension and mutual funds).
- They also have **professional management** or at least **higher-powered incentives** (pay-for-performance) compared to traditional SOEs.
- **Improved corporate governance** (external board members, more separation between ownership and control).
- **Financial transparency** (audited financials reported quarterly/semi-annually). Large flagship SOEs now choose BIG 4 auditing firms.
- Not all SOEs evolved into this model...

Petrobras (Brazil) 1980 vs. 2012

Equity (1980)
Government controlled
100% of votes



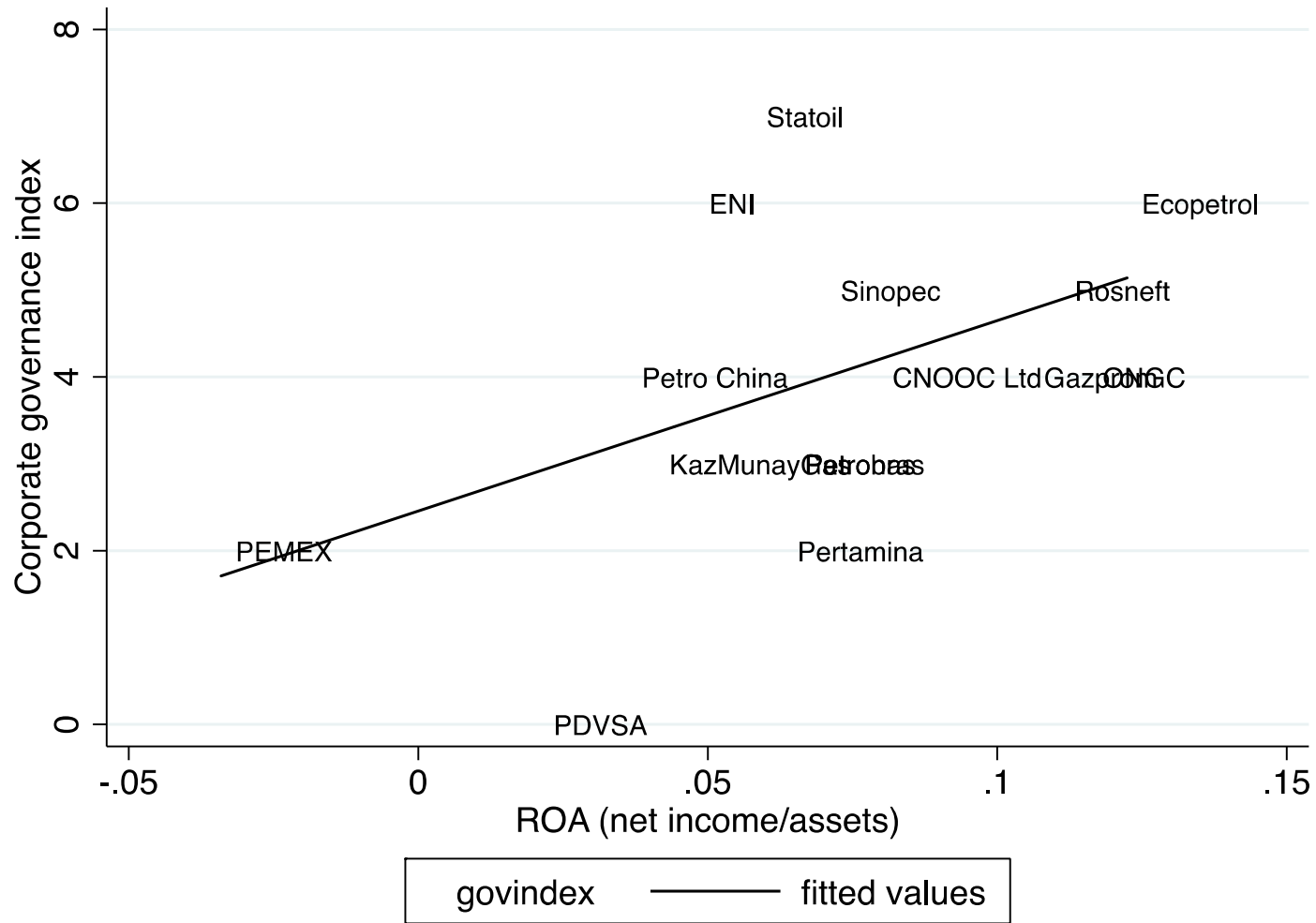
Total equity (2012)
Gov't controls 51% of votes



Corporate governance in 30 NOCs

NOC	Country	Listed NOC	Total gov't share of voting stock	Size of BOD	External board members	BOD members appointed by gov't	Board members term (years)	Gov't officials on BOD	CEO and chair of BOD are not same person	Chairman is an external board member & non-gov't official	Budgetary autonomy	External auditors	Governance index#
Statoil	Norway	Y	70.8	10	7	0	2	N	Y	Y	Y	Y	7
Eni	Italy	Y	30.3	9	3	0	3	N	Y	Y	Y	Y	6
Ecopetrol	Colombia	Y	89.9	9	6	3	1	Y	Y	Y	Y	Y	6
GDF Suez	France	Y	36.4	21	9	6	4	Y	N	N	Y	Y	5
Sinopec	China	Y	75.8	11	3	0	3	N	Y	N(**)	Y	Y	5
Rosneft	Russia	Y	83.0	9	3	0	7	Y	Y	Y	Y	Y	5
OGDCL	Pakistan	Y	85.2	11	8	n.a.	3	Y	Y	N	Y	Y	5
Saudi Aramco	Saudi Arabia	N	100	7	5	2	?	Y	Y	Y	Y	Y	5
Gazprom	Russia	Y	50.0	10	2	5	1	Y	Y	N	Y	Y	4
CNOOC Ltd	China	Y	66.0	11	5	0	3	N	Y	N(**)	N	Y	4
PTT	Thailand	Y	67.1	15	6+	0	3	Y	Y	N	Y	N	4
ONGC	India	Y	84.2	17	8	17	2	Y	Y	N	Y	Y	4
Petro China	China	Y	86.7	14	5	0	3	N	Y	N(**)	N	Y	4
Petrobras	Brazil	Y	55.7	9	2	6	1	Y	Y	N	N	Y	3
KazMunayGas	Kazakhstan	Y	62.0	8	3	5	3	Y	Y	N(*)	N	Y	3
Petronas	Malaysia	Y	100	16	7	9		Y	N	N	Y	Y	3
PDO	Oman	N	60.0	12	5	7	?	Y	Y	N		N(?)	2
KPC	Kuwait	N	100	15	11	3	?	Y	N	N	Y(***)		2

Governance and ROA in NOCs with financial transparency



Leviathan as a minority investor

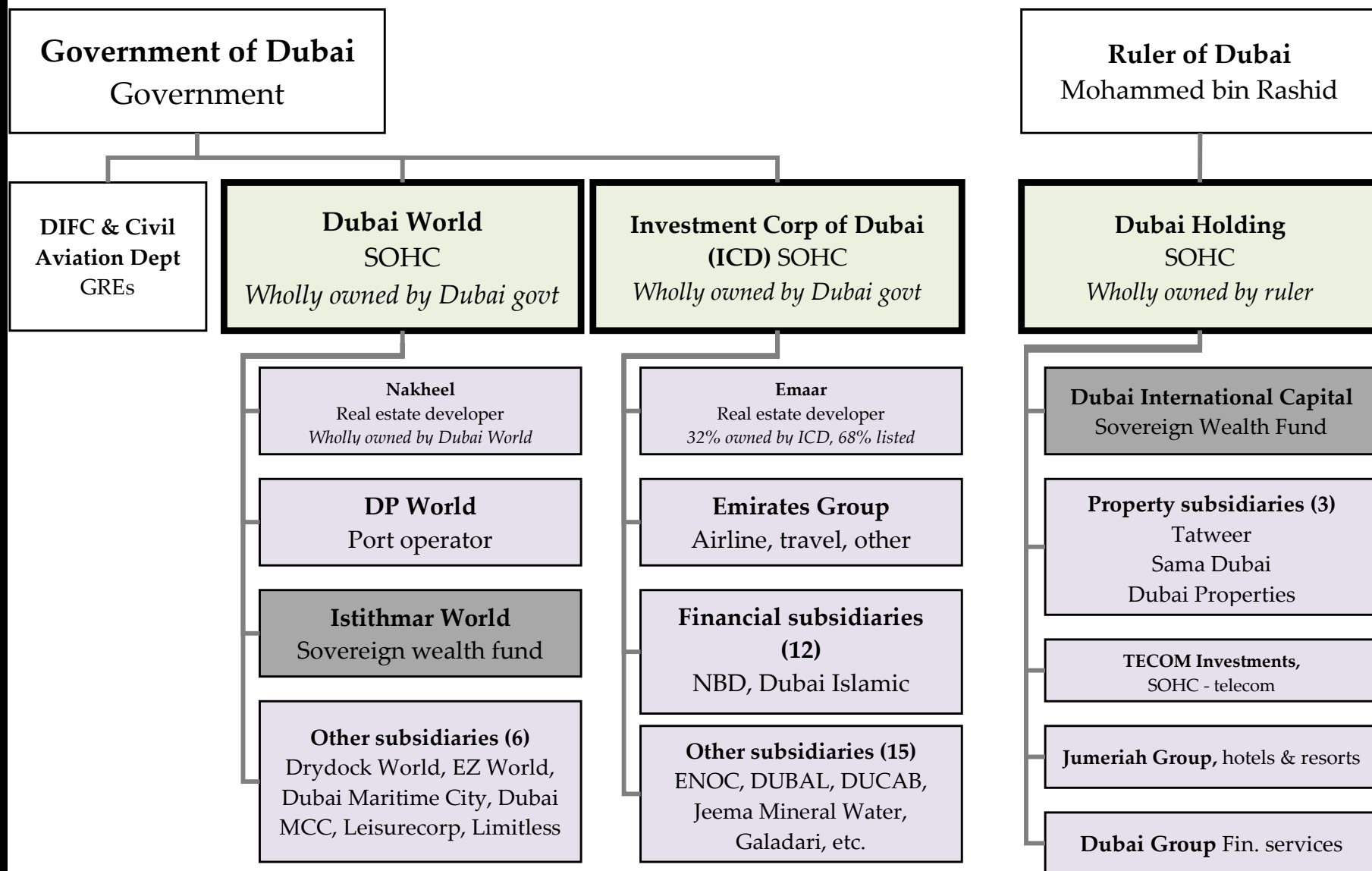
- Governments now have a large proportion of their investment in firms through minority positions (w/ or w/o golden shares)
- Gov't outsourcing management and monitoring of managers to private parties
- Minority investments can help firms overcome capital constraints
- This “model” of state capitalism is not well understood!

State-Owned Holding Co's and SWFs

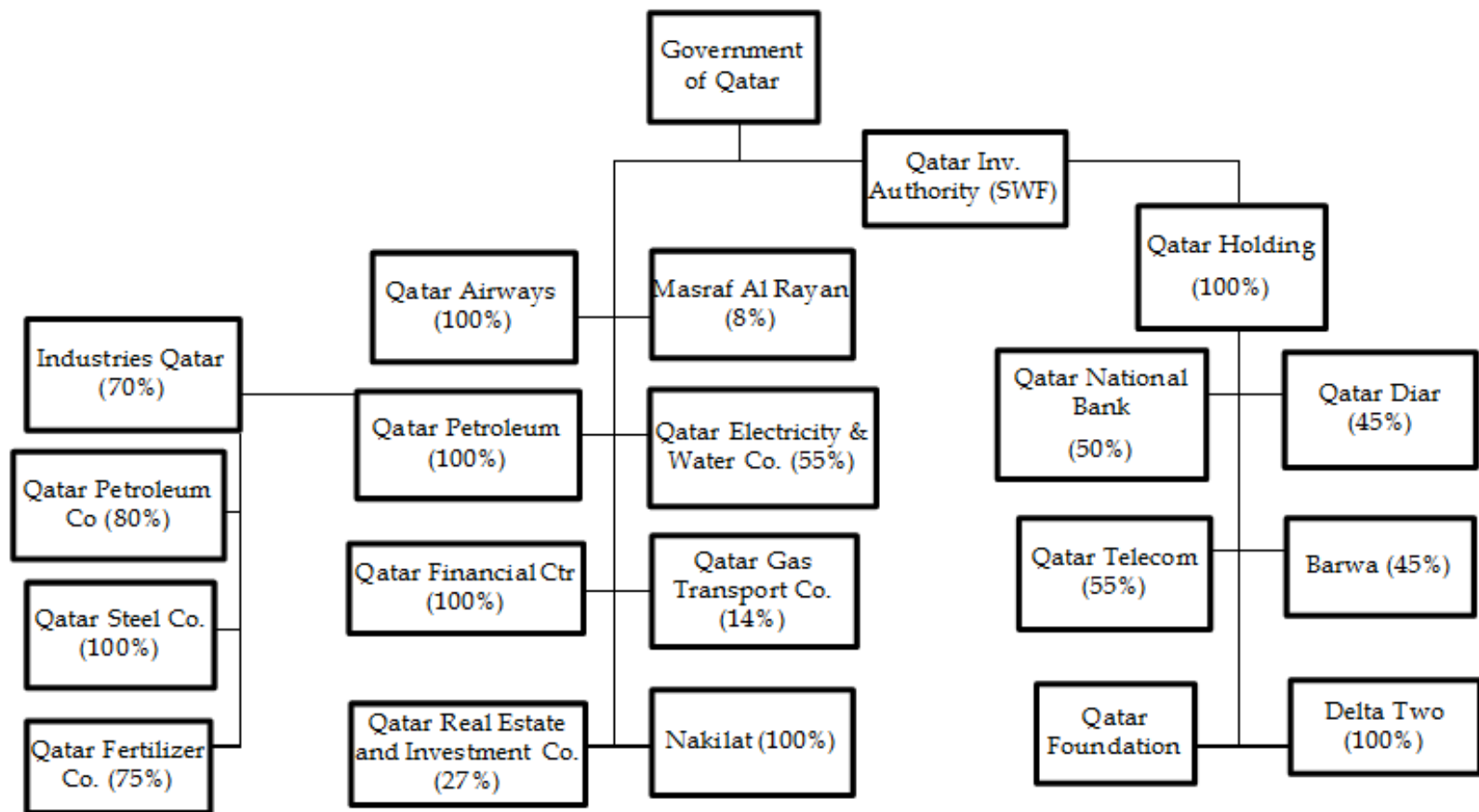
Governments use new vehicles to manage SOEs, often with professional managers & some degree of autonomy:

- Holding co's/pyramids → centralized or by sector (depending on complexity of industry)
- Development banks are also used as holding co's in Korea/Brazil
- Sovereign wealth funds also act as SOHCs in Qatar, Malaysia, Singapore, UAE, etc...

Figure 2 The Organization of SOHCs in Dubai, 2009



Source: Adapted from Morgan Stanley Report, Deutsche Bank Report, ThompsonOne, and SWF Institute. We thank Andrew Goodman for putting together this figure.



Source: Created with data from www.swfinstitute.org and Thompson One.

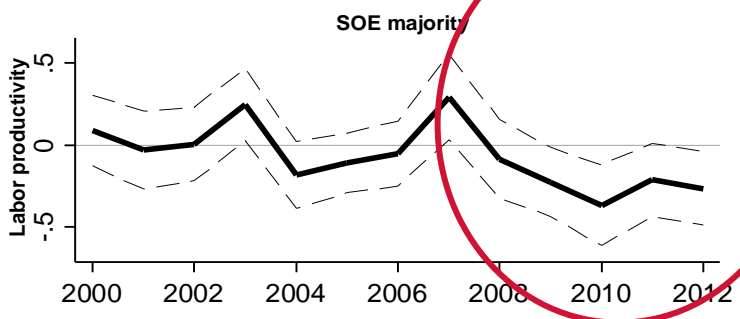
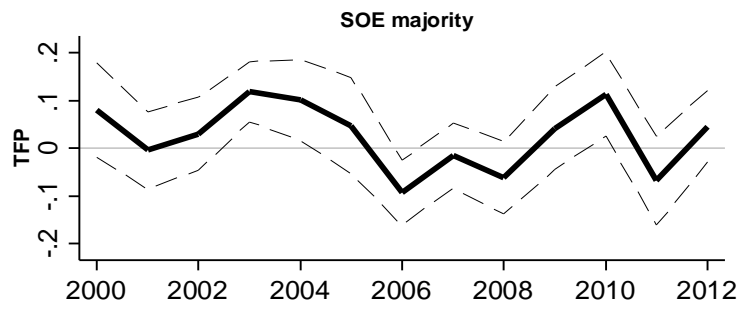
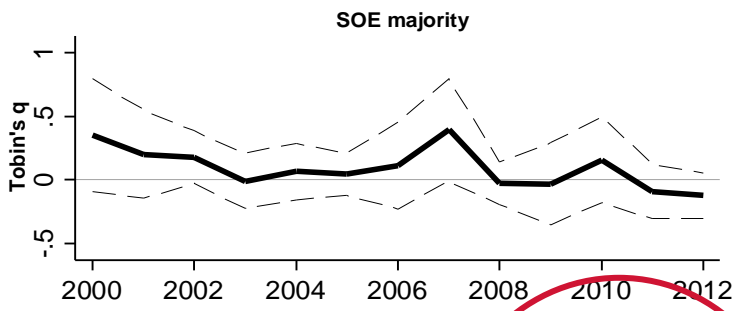
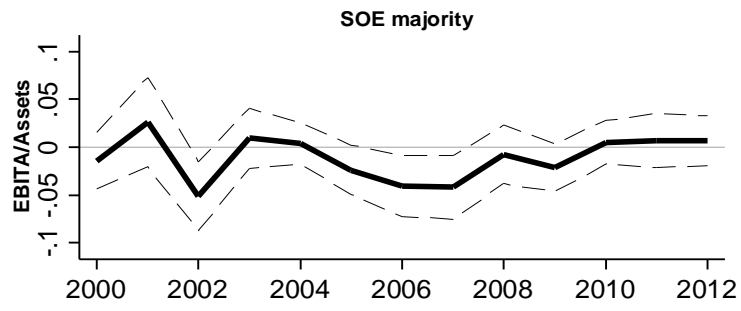
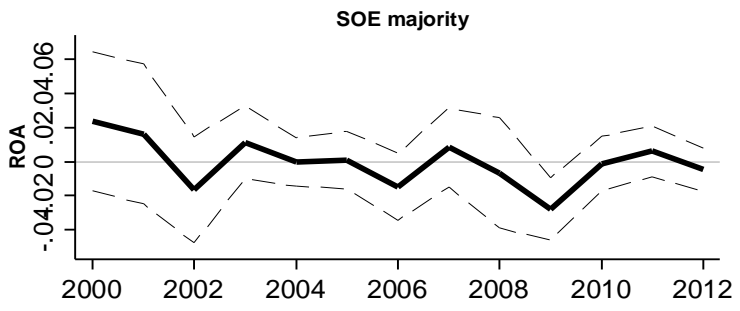
How do governments align management incentives in SOEs?

- China the CCP Central Organization Dept. controls promotions and creates levels/ranks for members (bonus on paper only)
- In countries with sophisticated stock markets, executives of SOEs have pay-for-performance compensation schemes
- In Gulf countries royal families run SOEs and SWF, but they also invest in SOEs (majority owned) and co-invest with SWFs... performance tied to family wealth

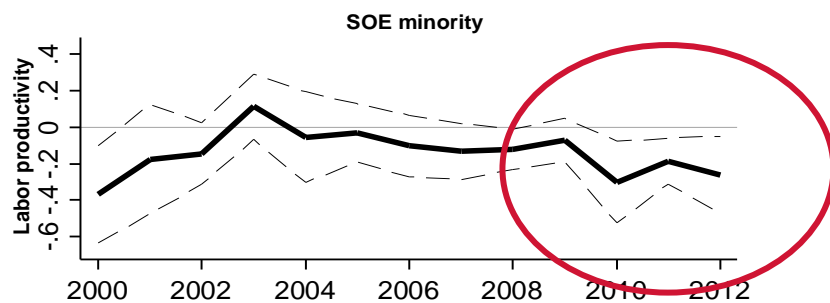
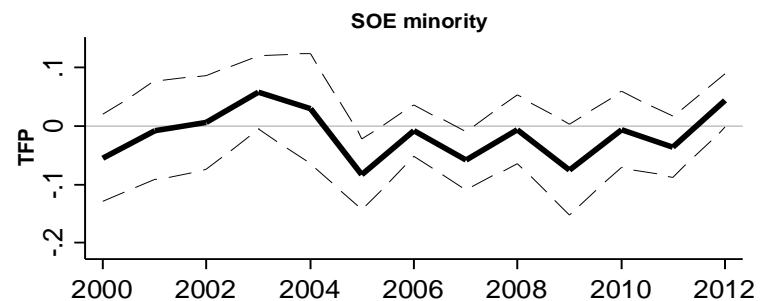
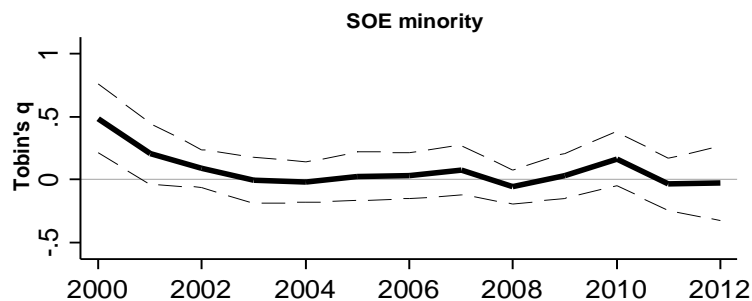
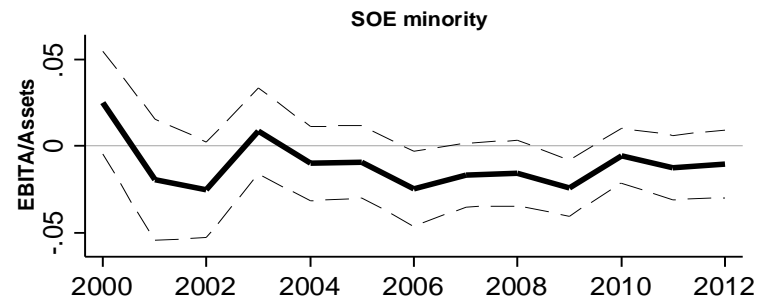
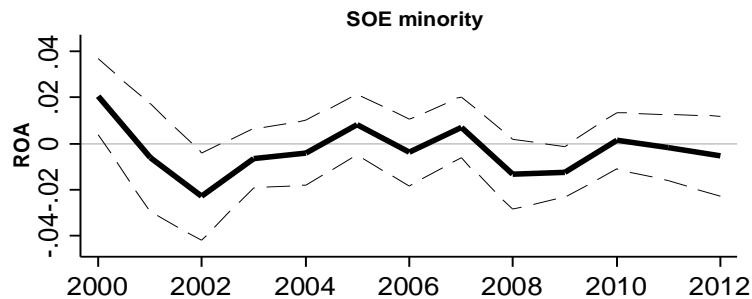
Outcomes of SOE reforms

- Little to no performance gap between SOEs and similar private firms
- Improved legitimacy of large SOEs (perceived as efficient/professional)
- Firms with minority government/SWF ownership considered solid investments (e.g., SWFs used as landmark investors in IPOs)
- SOHCs and SWFs considered LT investors solving market failure in many countries (e.g., Brazil the investment fund BNDESPAR)

No performance diff. bet. Hundreds of majority SOEs vs. similar private firms



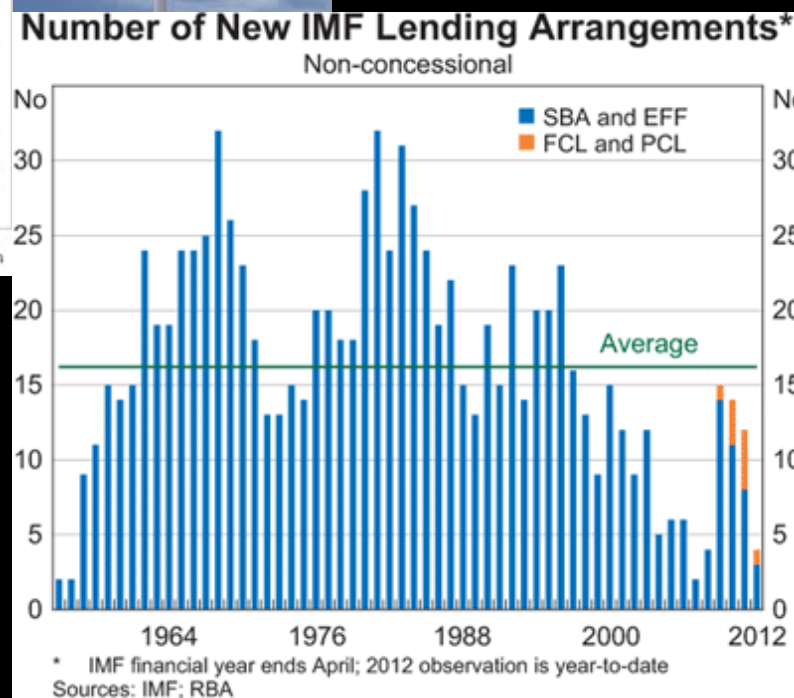
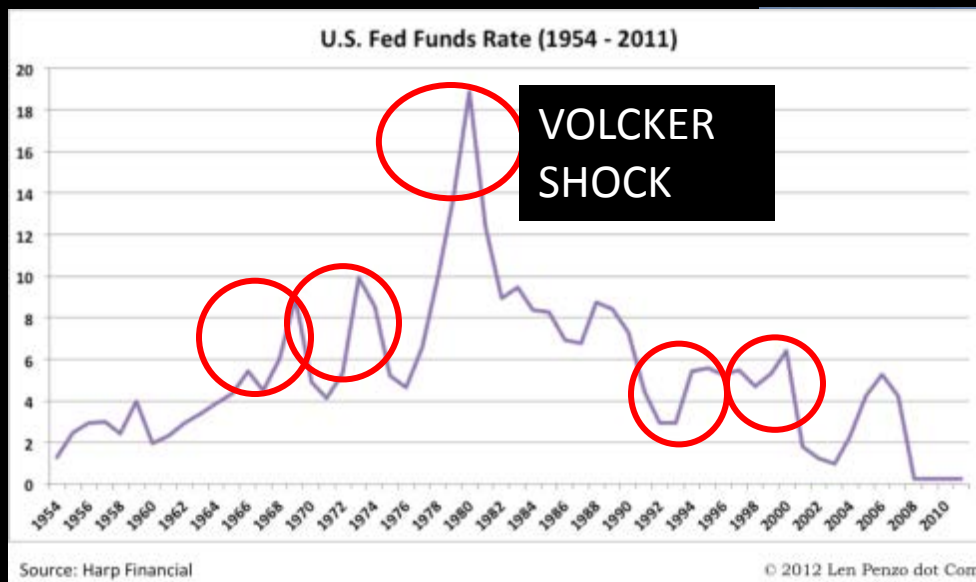
No performance diff. bet. Hundreds of minority SOEs vs. similar private firms



GLOBAL RISKS IN THE HORIZON

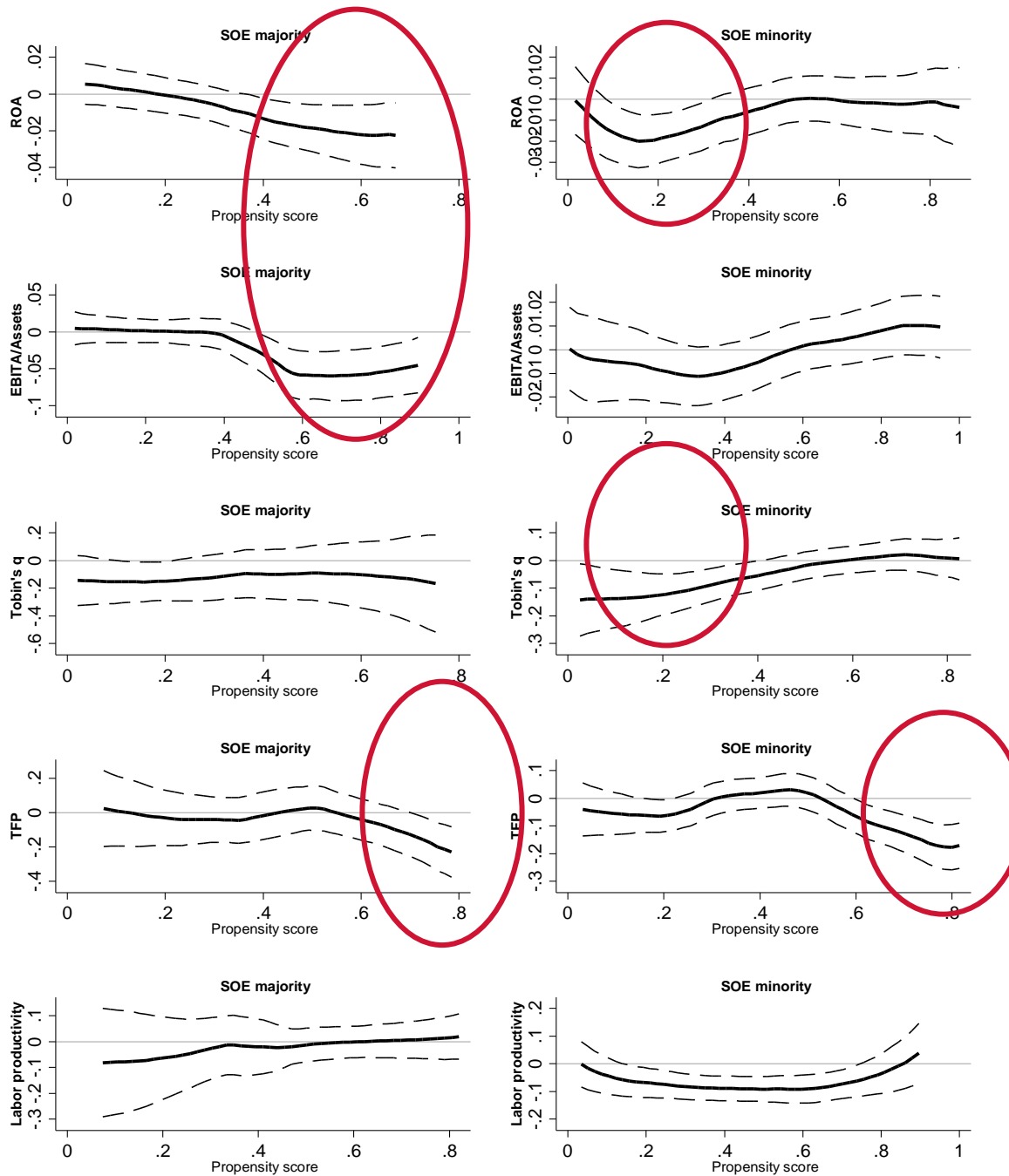
- IT was easy for countries to have a system of state capitalism when commodity prices were high (i.e., oil) and they were facing no binding budget constraint
- PROBLEM NOW is how to sustain the model with a binding budget constraint
- Can autonomy of SOEs and SWFs be preserved???

Bear scenarios: Big interest rate spikes and EM crises



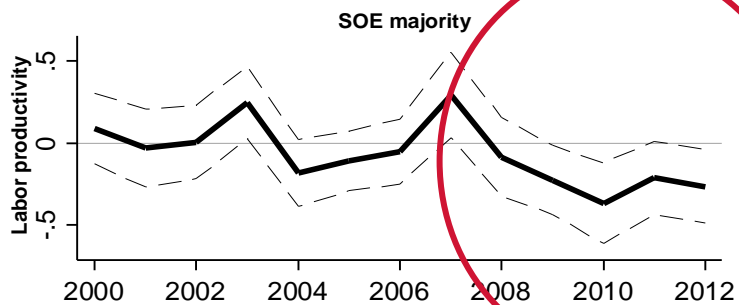
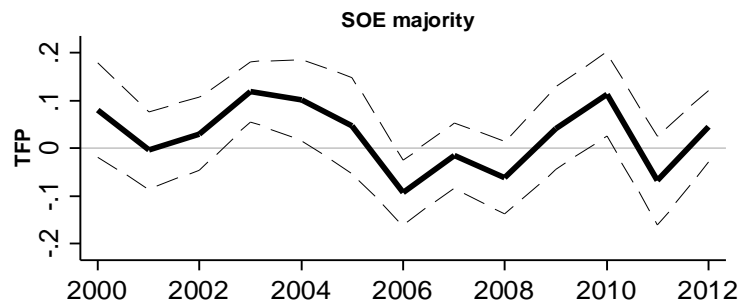
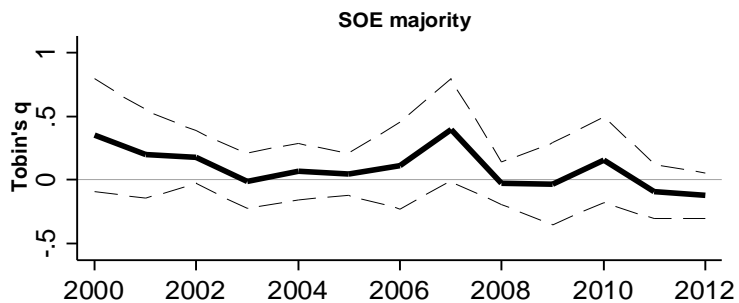
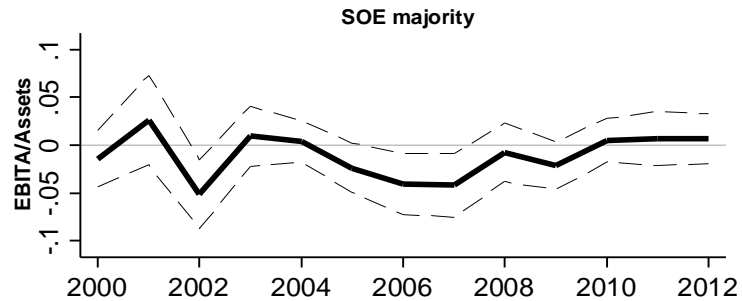
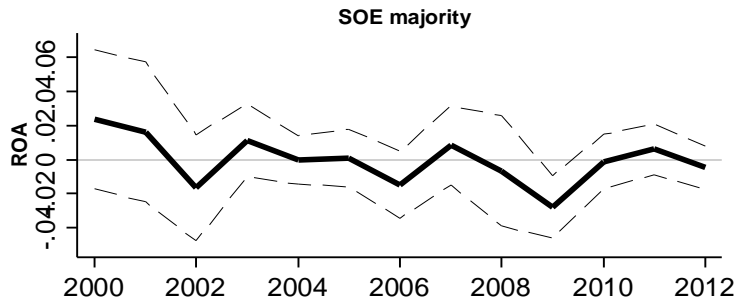
Binding budget constraints and state capitalism

- When the cost of capital for governments goes up, the opportunity cost of having a SWF goes up
- Are SWFs organized in a way that shields them from political intervention or from pro-cyclical policies?
- The same has happened with state-owned enterprises that have been reformed, during severe recessions they cannot fire workers at will and their performance vs. similar private firms opens up a gap
- The temptation of the government to intervene increases



- Performance of SOEs vs. Similar private firms during a severe crisis (two years of negative growth)

- Performance = ROA, EBIT/Assets, Tobin's Q, Productivity and total factor productivity



How to isolate SWFs from geo-economic events?

- It will be an issue of legitimacy!!!
- Governments have to feel it is illegitimate to tap those resources during tough times

SWFs need to

- Get clear mandates & financial/operational autonomy
- Introduce good corporate governance → checks & balances and a certain level of transparency
- Professionalize asset management + financial goals (meritocracy & isolation from politics/royal families)
- Show returns on foreign investments meet mandates and are responsible (no luxury/flashy purchases)
- Invest in infrastructure at home and highlight results
- Clarify that it is important to have state-owned investment vehicles to solve market failure, by making good investments at home

In national oil companies, political isolation & more checks and balances leads to more legitimacy and political isolation

	Statoil (Norway)	Petrobras (Brazil)	Pemex (Mexico)
<u>CEOs/incentives</u>			
CEO selected by	Board	Board (influenced by President of Brazil)	President of Mexico
Do CEOs usually change after presidential elections	No	In 3 out of 7 elections	Yes
CEO compensation has pay-for-performance component	Yes	Yes	No
<u>Financials/transparency</u>			
Autonomous budget	Yes	No, some investments need gov't approval	No, some investments need gov't approval
Listed?	Yes	Yes	No
Main institutional investors	Norwegian national insurance fund	Local pension funds, Black Rock	Bondholders & Ex-Im Bank
<u>Regulation</u>	Norwegian Petroleum Directorate (NPD), reporting to the Ministry of Petroleum and Energy, <i>de facto</i> independent	National Oil Agency (ANP), linked to the Ministry of Mines and Energy. However, influenced by the government	National Carbohydrates Commission (CNH in Spanish), a decentralized agency linked to the Ministry of Energy (SENER)

Thank you!

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