EXECUTIVE SUMMARY

Over the past decade, state-owned enterprises (SOEs) have doubled in importance among the world's largest corporations: at US$45 trillion, their assets are now 20 percent of the total. SOEs are present in virtually every country—numbering in the thousands, for instance, in Germany, Italy, and Russia. The recent growth of SOEs on the world stage primarily reflects the rise of China's economy—where SOEs still play a large role—along with other emerging market economies. SOEs often deliver basic services such as the water people drink, the buses they ride, and the electricity they need for daily life. SOEs such as public banks are also important sources of loans for families, farmers, and small businesses, particularly in emerging markets.

Yet, SOEs' hybrid status as neither government nor private—as well as their diversity in size, economic sector, and level of government responsibility—means that they are often overlooked, and many governments do not know all the SOEs they own or control. But, on occasion, severe problems in SOEs can contribute to economic slowdowns or recessions or the need for large bailouts from the government (among the Group of Twenty countries, recent examples include Brazil and South Africa). Therefore, governments should ask: Is each SOE the best vehicle to supply goods or services? If so, how can we guarantee that SOEs deliver value for taxpayers' money? And what policies can we implement so that SOEs compete fairly with private firms?

SOEs, taken as a whole, underperform. Drawing from a sample of about 1 million firms in 109 countries, this chapter finds that SOEs are less productive than private firms by one-third, on average. This diminished productivity can hamper economic growth, as some of the largest SOEs provide key inputs to the rest of the economy (for example, energy). Although SOEs are central to providing basic services to citizens in advanced economies, they are falling short in many developing countries, where more than 2 billion people remain without access to safe water and more than 0.8 billion lack reliable electricity. This often reflects SOEs' inability to charge sufficiently high prices to cover their costs and pay for the expansion of needed infrastructure. Moreover, many SOEs are plagued by corruption—both as recipients and as sources of bribes—domestically and across borders. Productivity of SOEs in countries with perceived lower corruption is more than three times higher than that of SOEs in countries where corruption is seen as severe.

This weak track record reflects governments' failures in many countries to establish proper incentives and promote greater transparency and accountability. Government demands of SOEs (that is, mandates) are often not clearly specified, costed, or appropriately funded. SOEs have also often been used to promote employment and to support credit growth without consideration for costs. In developing countries with high public debt, public banks hold more government debt than their private peers. Moreover, public officials or elected politicians may use SOEs to circumvent the government budget or to reward political backers with contracts, cheap credit, or jobs.

Government support for SOEs may also generate unfair competitive advantages over private firms. This concern has long been present in domestic markets, but, more recently—with the internationalization of SOEs and their large size—it has spilled across national borders. Domestically, some countries have frameworks that seek to promote fair competition between SOEs and private firms (for example, in Australia and the European Union). At the global level, however, there is no common framework.

How to Get the Most Out of SOEs

A core principle is do not waste public resources. Although SOEs exist for many reasons—including historical and political circumstances—it is important to regularly review whether the rationale for each SOE's existence and scope of activity remains valid and whether SOEs deliver value for taxpayers' money. For example, the case is weaker for SOEs that operate in competitive sectors, where private firms usually provide goods and services more efficiently. Privatization of such firms can bring benefits if the institutional preconditions are in place to ensure integrity of the sale and appropriate regulation of the privatized firm.

Effective frameworks for SOEs (many aspects of good practices are in place, for example, in the Nordic countries and New Zealand) include the following:

- *Full integration of all SOEs in the fiscal accounts:* This allows governments and the public to better assess the effect of SOE operations.
- *Provision of the right incentives:* SOEs should be able to set prices that reflect costs and should be compensated for mandates (for example, universal provision of electricity or water). Independent regulatory agencies can balance different interests (consumers, firms, and government).
- *Financial oversight and governance:* A first step is to collect information on all SOEs and provide clear mandates. Most countries can improve oversight and corporate governance.
- *Transparency of SOE performance and SOEs' relationship with governments:* An annual report analyzing SOEs' aggregate and individual performance (as in Brazil, India, and Sweden) can help.

Governments should ensure fair competition between SOEs and private firms domestically and globally to foster economic growth and use public money better. Many countries can do more to level the playing field, with direct benefits to their own economies. Globally, a potential way forward is to agree on principles to guide SOEs' international behavior (for example, transparency on government mandates and support) and recipient-country responses (namely, ensuring that SOEs are not discriminated against if they abide by the principles). Such principles would build mutual trust.

SOEs can help deliver on the global agenda by fighting corruption, contributing to greener policies, and supporting the pursuit of the Sustainable Development Goals. To achieve these objectives, many countries need more robust selection and oversight of their SOEs.