

Summary

Central government financial assets –
do they compute? (RiR 2015:16)



Central government financial assets – do they compute?

The Swedish National Audit Office has audited how the Government and Statistics Sweden report central government financial assets and liabilities, whether the reporting complies with reasonable transparency requirements and whether the valuation is relevant and of high quality.

General government financial wealth has traditionally not attracted much attention in discussion of economic policy. In recent decades the focus has been on keeping public finances in order. The surplus target and expenditure ceiling were the pillars of the fiscal policy regulatory framework. The framework has been developed further but the fundamentals are the same.

Central government debt has always been an important factor for investors who buy government securities, particularly if the debt approaches levels that create unease about repayment capacity. As the national debt ratio fell to what is regarded internationally as a low level, the question of national debt has attracted less attention in Sweden. In the euro area the trend has been the opposite and national debt has been an important question when framing economic policy in several countries.

Interest in public assets has been more limited, however, both internationally and in Sweden. Individual items have been discussed occasionally, but on the whole analysis of central government assets has been limited.

Audit background

Reasons: High quality and relevance of summaries of central government financial assets and liabilities are important from several perspectives. In the first place it is important to increase the insight that there are very great economic values in the State and that it is essential to manage them well. In the second place there is great variation between different estimates of the central government financial position and it is important to have a good picture of the values that are being handled. Finally, the balance sheet is part of the decision-support data for determining questions of inter-generational fairness.

Purpose: The purpose of the audit was to investigate whether the Government values, summarises and reports the financial assets and liabilities in a way that means they can constitute an appropriate basis for fiscal policy considerations and for decisions on individual matters.



DATE: 16-06-2015

Grounds for assessment: The Swedish NAO based its audit on the provisions of the Instrument of Government and the Budget Act. Under the Instrument of Government the Government administers and has at its disposal central government assets. The Riksdag decides on the fundamentals of administration and disposal of central government assets. Further, the Budget Act contains basic requirements for a high degree of effectiveness and good economy to be observed in central government activities. This assumes in turn monitoring and reporting of central government financial assets and liabilities that are adapted to these requirements.

Implementation: The audit was conducted on the basis of studies of various actors' descriptions of central government assets and liabilities. The work included interviews with representatives of the Ministry of Finance, Ministry of Enterprise and Innovation, Statistics Sweden and the National Financial Management Authority as well as document studies of Government Bills, the Central Government Annual Report etc.

Audit findings

It is necessary to measure the fair value of general government financial wealth

To obtain a fair view of the central government financial position and create the conditions for sound management of public funds, general government financial wealth should be measured at fair value in some context. An analysis and correct valuation of central government assets, particularly in a country with extensive assets, contributes to the provision of a well-documented picture of a country's general government financial situation. For a country like Sweden with major financial assets this is extra interesting as the picture of the country's financial position improves.

A central question for all decisions is what reference material is available. Adequate decision support data should include a good picture of the values that are at stake and the risks associated with the activity and thus the decision in question. This concerns both decisions on individual matters and on fiscal policy considerations on a more general level. The distribution between different generations is an example of the latter.

An important part of managing central government assets is identifying and managing risks in the assets. A risk assessment is often closely linked to the value of an asset. The greater the value the higher the risk, all else being equal.

Great variation in estimates

General government net wealth is calculated in various contexts with strikingly varied results. According to the financial items in the central government annual report, general government financial net wealth in 2014 was minus SEK 932 billion, while the financial accounts report minus



DATE: 16-06-2015

SEK 440 billion. The differences arise in that the definition of central government differs and the calculations are based on different valuation principles.

In the fiscal policy bills the Government's follow-up is mainly aimed at illustrating how the financial position will be affected by the expected budget outcome and forecast economic growth. As regards asset growth, future changes in value are by and large disregarded, despite the fact that historically they have accounted for a considerable part of asset accumulation. This does not give a reasonable view of the expected growth in general government and public sector assets.

What is to be presented in the central government annual report is governed by the Budget Act (2011:203), which allows the Government to largely determine the content and form of disclosures. The central government annual report aims to provide the Riksdag with material for follow-up and decisions as part of the governance of central government activities. This means for example that state-owned enterprises are valued using the equity method; in other words the central government share of the enterprises' adjusted equity.

In another publication from the Government, Verksamhetsberättelse för företag med statligt ägande (annual report for state-owned enterprises), another estimate is made of the value of state-owned enterprises than that in the central government annual report and the difference amounts to about SEK 120 billion.

There are great differences between the wealth reported in the central government annual report and that reported for the central government sector in the fiscal policy bills. This is because the calculations in the bills are in principle based on the financial accounts.

The fundamental purpose of the financial accounts is different from that of the central government annual report. The financial accounts endeavour to measure all financial assets and liabilities at market value. The financial accounts are a part of the official statistics and there is an international regulatory framework that governs their formulation. The Swedish NAO notes that Statistics Sweden has decided not to adhere fully to the overall principle of market valuation, but instead measures unlisted state-owned enterprises at equity value, which the regulatory framework does, however, allow. According to the Swedish NAO a market valuation in many cases gives a better picture of central government wealth.

An example of how different valuation principles generate different pictures of general government financial wealth is the treatment of unlisted state-owned enterprises. According to the annual report, general government financial wealth has risen by about SEK 60 billion since 2006 through an increase in value of these enterprises. The market valuation made by the Government of the same enterprises in the annual report for state-owned enterprises shows, however, that general government financial wealth decreased by more than SEK 200 billion in the same period.



DATE: 16-06-2015

No easily accessible picture

The fact that different information on the central government financial position appears in different publications may be confusing and for a layman it is probably difficult to understand why these differences arise. Differences in definitions and valuation principles make it difficult to obtain a complete picture of the central government financial position. No publication presents an easily accessible and overall picture. In the central government annual report there is certainly a comparison between how the Government and Statistics Sweden value the items in the central government balance sheet in a note but good previous knowledge is required to understand the information completely.

The regulatory frameworks that govern the financial accounts and the central government annual report have an impact on the results in a way that does not always promote a good overview of the central government financial position.

At the same time the audit of the financial part of the balance sheet shows that relatively few items account for most of the total financial value. For many of them there are valuations, albeit in different sources, that describe the fair value. Consequently the conditions for achieving follow-up that provides a better overview are good.

The Swedish NAO considers that the Government in some context should provide an overall and easily accessible picture of the central government financial position. Such an account should make it clear that there may be alternative pictures of the central government financial position. The purposes behind the summary should also be made clear, as well as how these have affected the choice of valuation principles and definition of central government.

Valuation and description of risks

The Swedish NAO's assessment is that the Government's reporting of risks associated with central government assets is unsatisfactory. Above all unlisted state-owned enterprises have low valuations. The fair values are often considerably higher, which is also shown by the valuations reported in the Annual report for state-owned enterprises. The method used for valuation of assets and liabilities affects the possibilities of making adequate risk assessments.

In many situations a market valuation of state-owned enterprises would constitute sound decision support. This applies to individual decisions that affect a state-owned enterprise, to monitoring general government financial wealth and to the ability to make a correct estimate of the risks in an enterprise.

As regards the liability side the Swedish National Debt Office has overall responsibility both for central government debt management and its risks, and for central government guarantees and their risks. For the asset side there is no agency with overall responsibility for management of assets and/or dealing with risks. Consequently the responsibility lies with the Government.



DATE: 16-06-2015

All in all, there are good reasons for both analysing risks and for providing the Riksdag and the general public with an overall description of the risks associated with the central government balance sheet. This description should include the consequences the overall risks may have for central government net capital, that is central government revenue and expenditure.

At the end of May the Government decided – after an announcement by the Riksdag – to set up a parliamentary committee to analyse the consequences for the Swedish economy of a changed surplus target. Part of this material may address the economic situation of the public sector. This includes valuation issues and if the surplus target was to be supplemented with a target for general government financial wealth, which for example has been discussed by the Swedish Fiscal Policy Council, the great difference between the central government annual report and Statistics Sweden's national accounts demonstrates the importance of definitions and valuation principles. Apart from the difference in financial wealth there are also differences regarding valuation of real assets. All in all, the difference between net wealth in the balance sheet and net wealth calculated in accordance with the national accounts principles amounts to as much as SEK 1 258 billion.

The Swedish National Audit Office's recommendations

- The Government in some context should provide an easily accessible picture of the central government financial position. Such an account should make it clear that there are alternative pictures of the central government financial position. By giving an overall description and clarifying the purpose of various summaries a clearer picture can be given of the central government financial position and how different valuation principles and definitions affect the result.
- The Government should provide information about the outlook for net capital and how the overall risks in the balance sheet may affect this outlook. This information should be a natural ingredient in the reference material for fiscal policy considerations.
- The Government should reconsider the purpose of reporting public wealth in fiscal policy bills.
- Statistics Sweden should present the market value of at least the larger unlisted state-owned enterprises in the financial accounts.

