

Talking Points

To own or not to own: Realising the value of public sector assets

Contents

<i>Introduction</i>	<i>2</i>
<i>How asset intensive is government?</i>	<i>3</i>
<i>An international perspective</i>	<i>4</i>
<i>To own or not to own</i>	<i>5</i>
<i>What's the purpose? Defining requirements</i>	<i>6</i>
<i>What is the most efficient delivery model?</i>	<i>9</i>
<i>Let's sell</i>	<i>13</i>
<i>Conclusion</i>	<i>14</i>
<i>About PwC</i>	<i>15</i>
<i>Contacts</i>	<i>15</i>

Introduction

The drivers of fiscal austerity will continue to frame decisions, and the ongoing reform of public services, for the rest of this Parliament. The Spending Review 2015 (SR15) has taken centre stage as the driving force behind the Government's commitment to control spending and 'finish the job of repairing Britain's finances', with a need to find £20 billion of further consolidation.¹

In the SR15 the Chancellor has emphasised the importance of casting the net of efficiency more widely, challenging government departments to "examine their assets and consider how they can be managed more effectively, including considering the role of privatisation and contracting out where assets do not need to be held in the public sector."² The starting point to address this challenge is to understand the asset intensity of government today.

¹ This is in addition to the £17 billion of savings announced in the Summer Budget, which included £12 billion of welfare cuts. HMT, 2015, Summer Budget 2015.

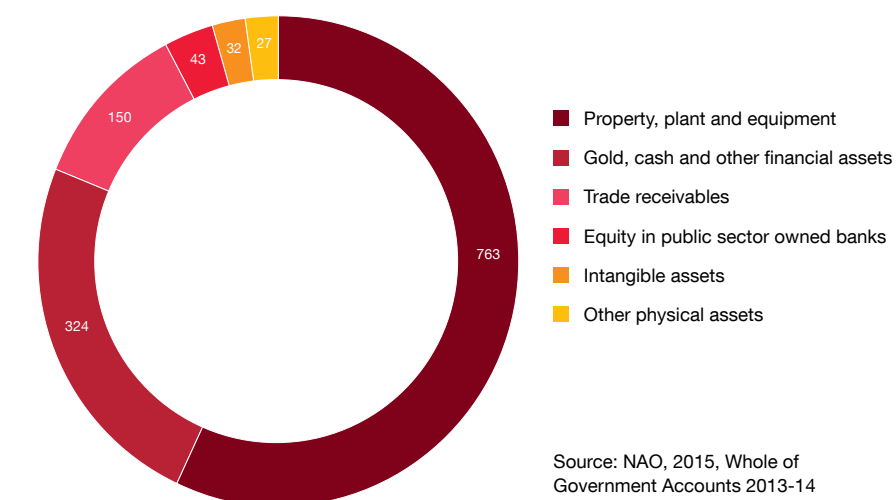
² HMT, 2015, A country that lives within its means: Spending Review 2015, p.20.

How asset intensive is government?

Government owns a wide range of assets, some of which are not those of its choosing e.g. shares in public sector banks, or held for 'national strategic reasons' e.g. gold and other financial assets (see Figure 1).

Even so, is this asset base of £1,300 billion the right size to support £700 billion of public spending? It is difficult to assess given the unique nature of some of the Government's assets and services. But it is worth noting that most private sector organisations, even the most capital intensive such as oil companies, have ratios of assets to revenues of less than 1:1, so the Chancellor is right at least to ask the question.

Figure 1: Public sector assets (£bn)



An international perspective

There is a common perception also of the UK as being a leading ‘privatiser’ with more of its assets in the private sector than other countries. The actual picture is more nuanced. We have used the Organisation for Economic Co-operation and Development (OECD) government expenditure data to compare spending patterns in fifteen developed countries to those of the UK in four key areas: education; healthcare; social services; and public safety.

This shows that the UK does have a strong history in some areas of providing services outside of direct state control, for instance, in post-secondary education. In primary and secondary education though, the UK experience is fairly typical of the OECD average though recent policies will likely shift patterns closer to the Scandinavian countries and their more decentralised education system. However, the UK ranks significantly behind other countries in educational support services being delivered outside public sector control.

The UK’s heavily publicly funded health system is a significant outlier compared to other nation’s insurance based systems. In public safety, no country has less than 95% of expenditure outside of direct public provision and investment. This presents an opportunity for new ideas to develop but with limited evidence of what has worked elsewhere. The UK continues to deliver significant proportions of social services (especially for the sick, elderly and family services) directly through public control. If the UK were to match the international average in each of these areas, £18.6bn a year would be streamed through direct transfers or for private/charitable deliverers rather than through public bodies.

To own or not to own

Although public sector organisations will, on a day-to-day basis, be aiming to make best use of the resources and assets at their disposal, SR15 provides an opportunity for all public bodies to stand back, take stock of their existing operations and assets and ask: do we need to be providing all of our current range of services. And are all of our assets still needed to enable a public service requirement to be met?

Where there is a public need to be fulfilled, it is clearly important to ensure that the organisation is deploying the most efficient delivery model which is effective in delivering the outcomes and value expected. As such, we look at a range of **different delivery model options**, including hybrids where the public and private sector venture together to deliver greater value from public sector assets.

As part of the assessment of delivery options, public bodies then need to ask themselves whether their most efficient and effective delivery model actually requires **public ownership of the current range of assets**. And where this is not the case, the final decision to be made is how these assets can be sold to obtain best value for the taxpayer.



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What's the purpose?

Defining requirements

At any one time government as a whole, and public sector organisations individually, possess different categories of assets which are used to deliver a particular set of services and outcomes. The starting point is therefore to take stock of these categories and challenge whether they are all required to meet a public need.

For instance, much of the recent debate in the wake of the sale of a tranche of the Royal Bank of Scotland shares has focused on the sale of shares below the price at which they were taken into state ownership. But it needs to be remembered that there was a very good rationale for government intervention – to support the financial system at the height of financial crisis. However, now that more normal times have returned, the requirement for government ownership has diminished.

Reasons for public ownership of assets

An asset comprises “a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.”³ The OECD and World Bank have set out a range of commonly stated reasons⁴ for state ownership of organisations and assets including:

- provision of public goods (e.g. national defence and public parks) and merit goods (e.g. public health and education), both of which benefit all individuals within a society and where collective payment through tax may be preferred to users paying individually and/or where a market failure under-provides an essential service
- limitation of private and foreign control in the domestic economy
- generation of income to increase public funds
- increase access to public services e.g. by selling certain good and services at reduced prices to targeted groups as a means of making certain services more affordable for the public good through cross-subsidisation
- encourage economic development and industrialisation e.g. sustaining strategic sectors (and perhaps improving labour relations), launching new/emerging industries, as an alternative to regulation, (especially where there are natural monopolies/oligopolies e.g. electricity, gas and railways) and controlling the decline of sunset industries, with the state receiving ownership stakes as part of enterprise restructuring.

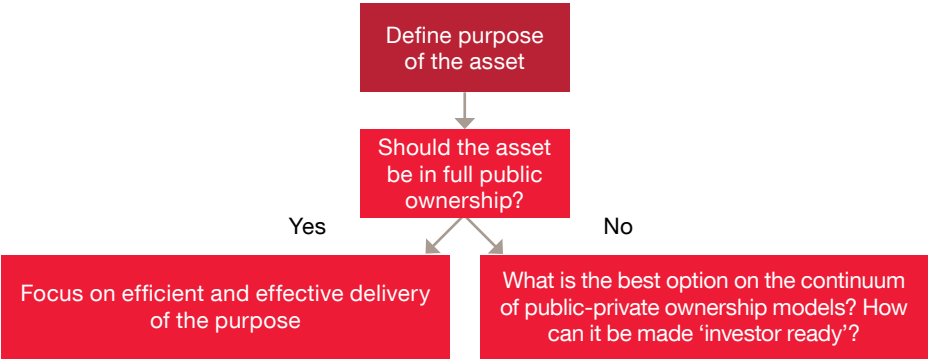
As such, returning banks fully to the private sector for the benefit of the economy is one of the key motivations behind the sale (alongside raising cash to reduce the national debt and reduce interest payments).

Broadening this out, there is a range of reasons for public ownership of assets at any given time, which also varies across a country's state of development (see **Box**).

Even the private sector can see reasons for an asset to be publicly owned. For instance, in PwC's CEO Pulse survey,⁵ private sector CEOs believed that government ownership has advantages in certain circumstances e.g. furthering social outcomes, providing physical infrastructure and creating stability in times of crisis within and across supply chains. But equally, there is a risk that **state ownership can destroy value if best practice in ownership and management are not applied**: CEOs in our Pulse survey were particularly concerned about inefficiency.

With the public sector (including local government) owning assets worth over **£1.3 trillion** (**Figure 1**),⁶ it is clearly right to ensure that optimum value is generated from the Government's balance sheet. There is, therefore, a need to shine a spotlight on the different types of assets that government holds and question whether the public sector remains the best owner i.e. the most efficient user of that capital, as part of SR15.

Figure 2: Key decisions for public sector managers



This means public sector managers asking themselves, for the assets they currently own (and the associated services provided):

- In the context of current government policy, what is the public service requirement we're fulfilling? For instance, is there a market failure, or other specific reason, which means that assets should be in public ownership?
- If there is a public need, what is the most efficient model to deliver the value and outcomes required?
- Does this delivery model require full public ownership of all of the current assets in the organisation?
- If some can be sold, how can most value be achieved from a sale?

It is important that these core questions are asked during the course of SR15 as the answers have important implications for action (see **Figure 2**).

This is particularly important in the case of land and buildings (see **Box**). A stated aim of SR15 is to continue the drive to reduce the size of the public estate, linked to a commitment to 'dispose of public sector land for at least 150,000 homes by 2020'⁷ with departments challenged to set out how they will meet their share of contributions to this target. This is also part of the drive to increase public service productivity which is to involve a “commercially-driven approach to land and property management across the central government estate”.⁸

³ IFRS Foundation www.ifrs.org/

⁴ OECD, 2005, “OECD Comparative Report on Corporate Governance of State-owned Enterprises”; The World Bank, 2006, “Held by the Visible Hand – the Challenge of SOE Corporate Governance for Emerging Markets”; Kowalski, P. et al (2013), “State-Owned Enterprises: Trade Effects and Policy Implications”, OECD Trade Policy Papers, No. 147, OECD Publishing.

⁵ Based on a survey of 153 CEOs in January 2015 on protectionism and government ownership. See <http://www.pwc.com/gx/en/ceo-survey/pulse/index.jhtml> for more details.

⁶ NAO, 2015, Whole of Government Accounts 2013-14.

⁷ HMT, 2015, A country that lives within its means: Spending Review 2015, p17.

⁸ HMT, 2015, 'Fixing the foundations: Creating a more prosperous nation.

The key question is whether changes in delivery models result in land not needed to meet public service requirements which can then be sold e.g. for development. Of course, there is a need to take account of the long term impacts of such decisions too – once the land is sold, it's gone for good. And there is always the risk of accusations of selling of the nation's assets too cheaply or in an inappropriate way. The public outcry over the proposed “privatisation of the forests” highlights some of the political sensitivities in this space.⁹

⁹ www.theguardian.com/environment/blog/2015/feb/17/privatisation-uk-woodlands-happening-by-backdoor

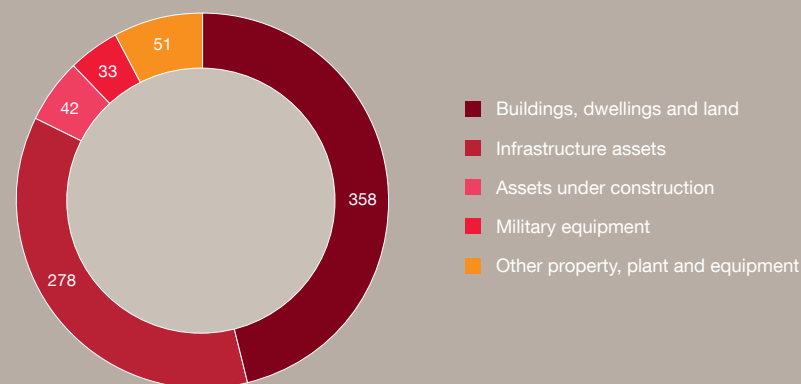
¹⁰ NAO, 2015, Whole of Government Accounts 2013-14

¹¹ www.express.co.uk/news/uk/423164/Winston-Churchill-s-War-Office-will-be-sold-to-raise-100million

The public estate

The Government owns around £350 billion worth of land, which comprises almost half of the £762bn of public sector property, plant and equipment assets in 2013/14¹⁰ (see Figure 3).

Figure 3: Public sector property, plant and equipment (£bn)



Clearly central and local government have significant property assets, while health trusts are also big owners of prime real estate. Many of these assets are sited in city centre locations, or up-and-coming urban areas, which could generate much needed funds through a sale, although care needs to be taken to evaluate the business case carefully. In particular, there is a need to weigh up the advantages to be gained e.g. in operational flexibility, against the risks, for instance, being locked into long and expensive leasing arrangements where there is known to be an ongoing need for the land.

Of course, not all of the opportunities arising from a fundamental review of the public estate will be as attractive as the sale, in December 2014, of the Old War Office building in London's Whitehall on a long lease arrangement.¹¹ But although few such prime publicly owned assets come on to the market every year, many other opportunities are likely to emerge, including the development of surplus land as more services are shared and/or co-located.

Any such deals are also not straightforward commercial transactions, being subject to normal government good practice in selling publicly owned assets and value for money assessments. They are also likely to attract significant public scrutiny, so it's vital to ensure that the potential benefits are shared between the seller and buyer. For example, if a prime asset is bought, refurbished and re-let there is an opportunity for the seller to agree a contract that offers a proportion of the profits on top of the proceeds from the sale.

What is the most efficient delivery model?

A considerable part of the public service reform agenda focuses on how to make public service delivery more efficient and effective including increasing digitisation and redesigning, sharing and integrating public services – the left hand side of Figure 2.¹²

Our focus here, however, is to look further at the right hand side of the decision tree in Figure 2 and ask what is the most efficient and effective delivery model if it is decided that the best future home for an asset is not in full public ownership.

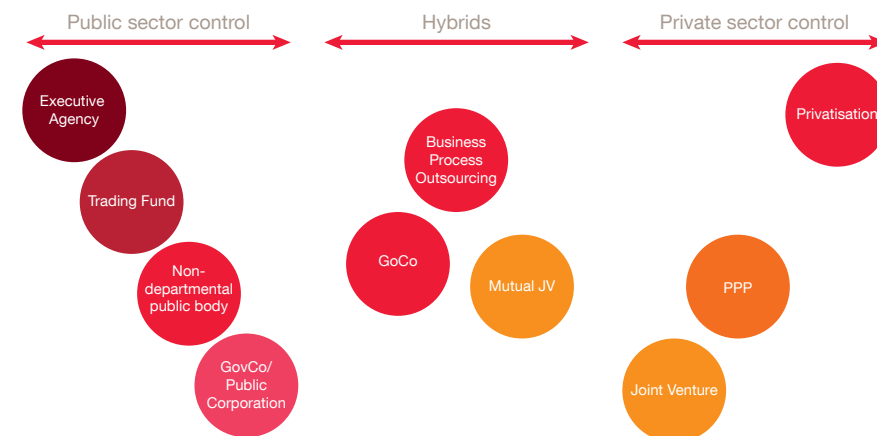
¹² www.pwc.co.uk/government-public-sector/publications/whitehall-matters.jhtml

¹³ Martin Jacobs, Financial Times 2 August 2015 - www.ft.com/cms/s/0/e4200b8c-379f-11e5-b05b-b01debd57852.html#axzz3kU3wlHkq

¹⁴ www.theguardian.com/business/2015/aug/08/64bn-question-george-osborne-left-to-sell-asset-sales?dm_i=2OYA,1N12,1F7JR,4IQ7,1

¹⁵ www.pwc.co.uk/government-public-sector/publications/under-pressure-securing-success-managingfailure-in-public-services.jhtml

Figure 4: Continuum of public-private models of control¹⁵



While top-tier stakes in assets such as RBS and Royal Mail will raise “big numbers”, the returns from sales of the next layer of operational assets would “present more limited potential for capital realisation. But there is also the opportunity for the private sector to make more innovative and creative use of these legacy assets.”¹³ In this next layer are organisations like Urenco, Channel 4, Royal Mint, Companies House, Land Registry, the Met Office and Ordnance Survey as well as part privatisation of the Green Investment Bank.¹⁴

It is important, therefore, to consider if private and/or third sector organisations can help to **release greater value from government's assets** and functions, including through privatisation and outsourcing, generating funds for other uses.

But privatisation and outsourcing are just part of a continuum of models of control which span the public-private interface (Figure 4). And **there is no ‘right’ answer** to the position of any organisation or asset on this continuum. Each option provides differing degrees of public ownership and influence. The key decision to be made is how value is optimised by **partnering with others**.

This range of models offers **choices for government**. There are, of course, no simple answers: there can be no ‘one size fits all’ approach. The choice will always depend on individual circumstances and context.

Although some will have an ideological commitment to private sector ownership, in practice we have observed that over time the mixed economy including part public/part private ownership (‘hybrids’) is becoming increasingly common as a stable, longer term arrangement. Indeed, nationally there are many examples of joint ventures where the private sector is introducing its commercial skills and making use of an asset which is under-utilised in the public sector (see **Box**).

Food and Environment Research Agency (Fera) joint venture

Fera provides scientific services to government and commercial customers, such as food retailers and manufacturers of crop protection products, in the UK and overseas, employing nearly 400 scientists at a site near York in northern England. It specialises in translating scientific knowledge into practical applications, such as helping to ensure food safety and quality ‘from farm to fork’, sustainable crop production, environmental management and conservation. It also plays a key role in the UK’s ability to respond to, and recover from, emergency situations affecting the food chain and rural economy (e.g. recent horse meat and ash dieback issues).

In support of the Government’s programme of commercialising certain public assets, Capita has acquired a 75% stake in the joint venture for £20m in cash, committed to making investments in the company which have been valued by the Government at £14.5m, and will use its infrastructure and expertise to enhance Fera’s ability to deliver scientific benefit to the public and return value to the taxpayer. Forecast commercial growth against specific, targeted markets is expected to enable the joint venture to achieve at least £700m revenue over its first 10 years. Growth will be generated through existing agreements with the public sector, securing new public sector work and by further developing services to achieve greater penetration of the commercial market. Fera already generates annual turnover of around £40m.

As part of the agreement, the joint venture has secured a long term service agreement for up to 10 years, to deliver services for Defra and a 10 year supplier framework through which scientific services can be bought directly by other crown bodies. The venture also includes the creation of a joint academic institute with Newcastle University aimed at advancing the understanding and application of science to practical agri-food problems.

There are also many successful examples from local government too, which is often at the leading edge of public sector practice. For instance, local government is collaborating with the Cabinet Office on “one public estate” which appears to be removing some of the barriers that siloed departments create.¹⁶

But continued budgetary pressures also mean that public bodies are increasingly looking to innovative ways of generating returns from their assets rather than selling them, particularly in local government (see **Box**).

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Local green energy

Bristol Energy¹⁷ has a mission to deliver reduced social inequality, improved environmental performance and sustainable economic prosperity. These core objectives are to be achieved by, amongst other things: focusing on locally generated, low carbon energy; providing a fairer deal for households currently on prepayment meters; supporting community investment in renewable and low carbon projects; developing district heating, electrical distribution and broadband/digital networks; and protecting the city’s critical infrastructure, thereby improving energy security and resilience.

The aim is for Bristol Energy to support the business of the Council, generating a new revenue stream for the Council to reinvest into the City. The launch of Bristol Energy while Bristol is European Green Capital potentially provides a vehicle to promote the city globally and attract both public and private investment by showcasing Bristol’s commitment to sustainability and energy.

Of course, there are again pros and cons: just witness the debate on whether parking charges help or hinder visits to the high street, and therefore whether the wider economic benefits more than offset the loss of direct income to the council.¹⁸ While it is always important to question whether organisations should

be investing in apparently ‘non-core’ activities, there are assets which need to be in public ownership to fulfil a public need but which are not always fully utilised, creating spare capacity from which more value can be released to the benefit of the public purse (see **Box**).

¹⁶ www.local.gov.uk/onepublicestate/-/journal_content/56/10180/6678286/ARTICLE

¹⁷ www.bristol-energy.co.uk/

¹⁸ www.conversation.which.co.uk/transport-travel/parking-enforcement-charges-fines-town-centre-high-street-shops/

Letting of the Marchwood concession

Marchwood Sea Mounting Centre (the Port) is a 91-hectare port facility near Southampton which provides the Ministry of Defence (MOD) with a sea-mounting capability, and is used for sending materiel to and from overseas. The commercial attractiveness of the asset to the private sector includes its location, proximity to major European shipping lanes with deep water access, rail access and substantial land space for development. MOD announced its intention to sell the Port following the 2010 Strategic Defence and Security Review and during a period of preparation it established the future military requirement from the Port, engaged extensively with the potential investor market, and identified a preferred structure for the transaction.

Following a competitive sales process MOD selected Solent Gateway Limited to enter into a long term concession to manage and develop the commercial potential of the Port. As part of the arrangement Solent Gateway Limited will deliver MOD's requirements and subject to delivering these it has the right to develop and exploit the commercial potential of the assets and land. With the Port not currently being used to its full capacity, this arrangement is expected to generate significant value for the MOD, in terms of both the profits generated by using the spare capacity at the Port, and a reduction in the cost of sea-mounting. The commercial arrangement secures the delivery of MOD's routine and, importantly, surge requirements. The new Port operator will also provide a deployable Reserve capability as part of the Army's Total Support Force initiative.

And this is not just about infrastructure, although it's easy to visualise the challenge in terms of physical assets. It's also crucial to think of public assets in their broadest sense, taking a fresh look

at how value can be unlocked from more intangible assets like public data, intellectual property, collective purchasing power and people's skills (see [Box](#)).

¹⁹ FT.com, 22 June, 2015

Commercialising knowledge

A radical idea would be for government at all levels to commercialise its greatest asset: the knowledge base it has created over years of public service delivery. Public servants have an impressive stock of expertise that is highly regarded both internationally and by the private sector. This includes leading practices in areas such as social care, justice and policing. What's more, this is expertise for which a clear market exists.

The challenge facing the Government is to identify, protect and commercialise its expertise, held as Intellectual Property, so that it can earn revenue from it. There are pockets of good practice already in existence. For example, Axelos, a co-venture with Capita, exports training schemes designed in Whitehall to private sector clients worldwide. It shows what can be achieved when government cooperates with commercial organisations to exploit the value of its knowledge base.¹⁹

Let's sell

The Chancellor has already set out a clear direction of travel, with the challenging target of raising £32bn in asset sales in 2015-16. Further sales of RBS and Lloyds Bank shares will be key to generating the bulk of this (alongside UK Asset Resolution, the Student Loan Book as well as Royal Mail).²⁰

²⁰ www.ft.com/cms/s/0/d9b48228-18b8-11e5-8201-cbdb03d71480.html#axzz3kU3wlHkq

²¹ www.ft.com/cms/s/0/82a26238-3222-11e5-91ac-a5e17d9b4cff.html#axzz3kU3wlHkq

Figure 5: The transactional life cycle



Clearly changes to the Government's asset base need to be made in a sustainable way, with an eye to the long term including the impact on markets and competition and the continued efficient delivery of the associated public services. In the push to release the value of assets as part of a time constrained Spending Review, care also needs to be taken not to engage in a fire sale of the nation's assets and accusations of selling the 'crown jewels'.

As John Manzoni, Chief Executive of the Civil Service, notes Whitehall must "avoid short term cost-cutting actions which may make it even harder in the future".²¹ However, if the decision is taken to sell (in full or part), the key

question then becomes how to drive best value for the taxpayer. In particular, there is a need to design and deliver an efficient and effective transaction process and timetable aimed at maximizing competitive tension and minimising costs (see [Figure 5](#)). As part of this process, there are some key activities such as modelling the trade-offs between up front proceeds versus longer term value for money while also identifying the right structure for the transaction.

It's also important to package the asset in a way which is attractive for the private sector to invest.

Conclusion

There are many cyclical and political trends at work when it comes to maximising the value of public sector assets. So there is no universally ‘right’ answer. Instead, government at all levels needs to go back to its purpose and assess whether there is a public service requirement that requires ongoing public ownership of assets, or not. If the answer is that assets should be retained in public ownership, there is clearly an important job to be done to ensure value for money, with efficient and effective service delivery and new business models delivering better outcomes for less. Of course if the answer is that an asset should be moved out of the public sector (in part or in full), there is then a need to choose the right option from the range of alternatives and ensure that the assets are ‘investor ready’. There is also a need to follow through and pay attention to realising the full potential benefits from any sale. The reality is that if the value of assets is to be maximised, there needs to be innovation and appropriate risks taken. By building the capability, being pragmatic, identifying the right partner and putting in place the right rewards and incentives, the chances of success are increased.



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PwC provides assurance, tax and advisory services to the public sector. Working together with our clients – across local and central government – we look for answers on how to increase efficiencies while improving quality and outcomes, and help to develop solutions that add value and are practical to implement.

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