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The Motives for Issuing Exchangeable Bonds in the Privatization of State-Owned Enterprises

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Abstract

Using a unique sample of exchangeable bond issues carried out in seven countries since the 2000s, this paper investigates the role of hybrid debt in the privatization of state-owned enterprises (SOEs) via government-controlled investment vehicles. This research shows that so far, sixteen series of exchangeable bonds amounting to approx. USD 25 billion were issued to privatize ten SOEs in the telecommunication, energy, basic materials, industrials, healthcare, and utilities sectors in Europe and Asia. Moreover, in some cases, the privatization of SOEs by means of exchangeables can prove to be a more favorable alternative to traditional methods of selling shares directly on the capital market, for example, via IPOs or SPOs (during periods of deep undervaluation of privatized companies or of high stock market volatility). First, shares can be sold at a later date and at a higher price. Second, the impact on the stock market price of an SOE may be less disruptive to shareholders. Third, the entire privatization process tends to be more flexible for issuers in that they can perceive exchangeables as a source of relatively cheap, long-term external capital while keeping control over the privatized company until the potential conversion of debt by bondholders.

Keywords: state-owned enterprises, privatization, equity-linked securities, exchangeable bonds

JEL: G32, G34, G38, L33



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Introduction

Privatization, defined in the simplest way as the government divestiture of state-owned enterprises (SOEs), has been the subject of intensive research by academics and policymakers over the past three decades. Its primary aim is to reduce the government's role as a dominant stakeholder in the domestic economy and to increase the importance and involvement of the private sector. According to the most current OECD statistics, privatization revenues have more than doubled over the last decade, from around USD 110 billion in 2008 to USD 266 billion in 2016 (OECD 2019).

In the last twenty years, SOEs have been among the largest and fastest-growing multinational enterprises. However, in-depth research in this area is limited and depends heavily on the definition of SOEs adopted in each study (Capobianco and Christiansen 2011). Nevertheless, Kowalski et al. calculated in 2013 that one in ten of the 2,000 largest globally-listed companies of 2011 were state-owned. The IMF's estimates show that this share has risen to 20% in the past decade, and the assets of SOEs worldwide are nowadays worth \$45 trillion, which is more or less half the global GDP (IMF 2020). SOEs are gaining importance primarily in emerging market economies, while in developed economies, their significance has remained stable. In OECD countries, state-owned enterprises usually operate in sectors identified as strategic for the national economy, such as energy, rail transport, finance, and telecommunications (OECD 2020).

Several studies documenting smaller productivity and value destruction in state-owned firms provide arguments for reducing public ownership and changing corporate governance in SOEs (Harrison et al. 2019). Such action may primarily support the business management process and positively affect their financial results (Djankov and Murrell 2002; Brown, Earle, and Telegdy 2004; 2016; Estrin et al. 2009). SOEs significant inefficiency and poor performance can be explained by various factors, including strong political interference in the decision-making process of political-oriented managers (Shleifer and Vishny 1994; Boycko, Shleifer, and Vishny 1996; Sheshinski and López-Calva 2003) or inadequate monitoring of management, which incentivizes them to follow their own objectives (Vickers and Yarrow 1991).

On the other hand, some recent studies indicate that privatization enhances corporate social responsibility (CSR) performance and leads to increased CSR investments (Bou-bakri et al. 2019). However, this observation has not been proven in all countries (Khan et al. 2021). Moreover, privatization can be beneficial from a state perspective. Revenues from privatization can supply state budgets and help reduce budgetary deficits (Megginson and Netter 2001), as well as advance the development of domestic financial sectors and capital markets (Boutchkova and Megginson 2000). However, it should be noted that an excess of state ownership beyond a certain point can contribute to a reduction

in firm-level stock liquidity (Boubakri et al. 2020). Privatization is a highly politically sensitive process exposed to potential corruption and abuse, owing to its involvement in the transfer of productive assets from state to private hands. It must therefore be carried out very carefully and requires politicians to thoroughly analyze all factors that can significantly impact the privatization process and enhance the country's economic growth (Estrin and Pelletier 2018).

Privatization can be carried out: (1) By the SOEs themselves involving their own internal structures and resources; (2) Through the divestment of shares directly by the state; or (3) By selling corporate assets owned by the state indirectly via government-controlled investment vehicles.

There are three main methods of privatization that depend on, among other factors, the size of the SOEs, current market conditions, financial market maturity, the degree of competitiveness of privatized economic sectors, the domestic legal systems, and political context (Estrin et al. 2009; OECD 2019). The first method embraces trade sales carried out through private placement or by trade sale auctions. They both involve selling shares to favored bidders or offering tranches of shares in already listed SOEs to groups of preferred private investors. The second method is based on management or employee buy-outs (MBOs or EBOs), which involves selling shares to legal entities controlled by management or staff. The third way encompasses the sale of shares on the capital market through initial and secondary public offerings (IPOs and SPOs), accelerated book building (ABB), or by issuing hybrid debt, which can be converted or exchanged for SOE shares. A common purpose of such issues is simply to dilute state ownership in SOEs.

The privatization of SOEs using hybrid debt instruments, such as bonds with warrants, convertible bonds, and exchangeable bonds, is particularly interesting from an academic point of view. Due to the discernible gap in the literature, special attention should be paid to the divestments carried out through exchangeable debt. This instrument is usually analyzed from the perspective of private entities (Ghosh, Varma, and Wollridge 1996; Danielova, Smart, and Boquist 2010; Danielova 2011), ignoring its role in the privatization of state-owned companies. Few theoretical articles focused on specific case studies on the privatization of SOEs (Kaźmierczak and Marszałek 2013). In fact, they do not find the motives behind the issuing of exchangeable debt in privatization, nor do they indicate the advantages of this instrument compared to traditional methods of disposing of state ownership, such as IPOs, SPOs, or trade sales. It is also not clear how exchangeables help managers to improve the operational efficiency of state-owned enterprises by gradually increasing the participation of private investors. All previous conclusions were primarily drawn from an extrapolation of the results from studies on other forms of hybrid debt, such as convertible bonds used by private entities and not for privatization purposes. In light of this consideration, it can be assumed that privatization through exchangeable debt may be carried out to gradually privatize and sell

a minority block of shares among small investors (Ruozi and Anderloni 1999), especially in a period of deep undervaluation and large fluctuations in the stock market (OECD 2019). However, all these suppositions call for empirical verification.

The intention of this paper is to fill in the above-mentioned research gap. It aims to identify motives for issuing exchangeable debt in the privatization of SOEs from the perspective of corporate finance management and indicate possible advantages of this approach over the traditional ways of selling state ownership. Analysis of the unique research sample, which comprises sixteen exchangeable issues carried out in seven countries since the 2000s, led to answers for three key questions: 1) How common are exchangeable issues for privatization purposes over the last two decades? 2) What motivated the public party to use hybrid debt instruments as a favorable alternative to traditional ways of selling shares of state-owned firms? 3) How are the exchangeable issues that are used to privatize SOEs designed?

By addressing these research questions, the paper contributes to the literature in several ways. First, its main findings are in the line with mainstream research on the use of hybrid debt instruments. Second, it provides insight into potential reasons for issuing exchangeable debt during privatization. Third, it complements knowledge on issuing exchangeable bonds among business entities and supports managers in corporate finance management.

The rest of the paper is organized as follows. A literature review is provided in Section 2, while Section 3 describes the data collection and the sample selection process. Section 4 presents the analyses and discusses the results, and Section 5 concludes the paper.

Literature review

The unconventional construction of hybrid instruments makes them a useful tool when divesting private entities. Knowledge about them is scarce due to the relatively low popularity of exchangeable bonds when privatizing SOEs in the public sector. The only article on the use of exchangeable debt in privatization includes a description of the mechanism of state property divestment of SOEs based on specific case study examples in different countries (Kaźmierczak and Marszałek 2013).

Privatization by means of hybrid debt instruments can take various forms. First, state ownership can be disposed of through debt-equity swaps. It involves the exchange of sovereign bonds or bank loans for ownership rights to equity, helping governments to reduce their foreign debt burdens¹ (Ganitsky and Lema 1988; Ramamurti 1992; Bowe and Dean 1993; Mil-

¹ Exemplified by debt conversion programs in Latin American countries in the late 1980s and early 1990s.

man 1996). Second, it can be done by privatization bonds, which are sovereign bonds that give bondholders the priority to convert them into shares of privatized enterprises² (Khosrowshahi 1997). Third, privatization can be carried out directly by privatized companies by issuing bonds with warrants or convertible bonds that can be converted for their shares. They can take the form of going-public bonds. These instruments are issued prior to a listing of privatized companies on a stock exchange, and bondholders have the right to convert them for shares during the IPO at a predetermined price (Lieberman and Kirkness 1998). Fourth, privatization can be carried out by exchangeable bonds via government-controlled investment vehicles, such as dedicated state agencies, sovereign wealth funds, development banks, and government-owned investment funds (Każmierczak and Marszałek 2013).

Exchangeable debt is a hybrid instrument similar to convertible bonds. The main difference is that exchangeables can be exchanged for a company's existing shares owned by the issuer, not for the shares of an issuing company, as in the case of convertibles. There are a number of arguments that point to the advantages of share disposal using hybrid debt instead of the ordinary sale of common stock on the capital market. Most of them may be crucial for the privatization of SOEs.

First, issuing exchangeable debt can be more cost-effective for the issuers because they avoid the complex and time-consuming procedure of issuing SOEs' shares through IPOs or SPOs (Barber 1993; Gentry and Schizer 2003; Kleidt 2006). Second, the announcement of exchangeable debt offers may be associated with a less negative price response of the privatized firms' stock than the response when the ordinary sale of equity on the public capital market is announced (Ghosh, Varma, and Wollridge 1990; Barber 1993).³ Third, by issuing exchangeable bonds, the issuer may avoid issuing undervalued shares of a privatized company and selling them at a higher price at a later date (OECD 2019). Fourth, issuing exchangeable bonds does not affect the ownership structure of the issuer because the bonds can be converted into common shares of its subsidiary. As a result, the issuer does not need to recognize gains on the sale of shares and can capture all dividends paid by the underlying company until the conversion of debt (Barber 1993). Fifth, due to the embedded conversion option, the exchangeable bonds may constitute a source of cheaper medium- and long-term financing for the issuers (Lieberman and Kirkness 1998).

A simplified scheme of privatization through exchangeable bonds is shown in Figure 1. The process typically begins with the issuing of bonds that are exchangeable for SOE

² As seen in Morocco in the mid-1990s.

³ Possibly due to the repurchase guarantee embedded in the exchangeable debt offering. The issuing firm guarantees that it will keep the stock of underlying firmstock if its value falls below the value of the straight bond component of the exchangeable offering (Barber 1993, p. 57). However, other analyses reveal that exchangeable offerings convey unfavorable information about the underlying firms to the market and may be interpreted as the beginning of restructuring process (Amman, Fehr, and Seiz 2006; Kleidt 2006; Danielova and Smart 2012).

shares, usually by a government-controlled investment vehicle. Bonds are subscribed mostly by institutional investors. Depending on the strategy, the proceeds from the issue remain with the SPV, are transferred to the SOE, or are redirected to the state budget. At maturity (or earlier if the bonds have an embedded call option that allows investors to convert debt into equity before maturity), investors decide to exchange bonds for SOE shares and become shareholders in the privatized company.

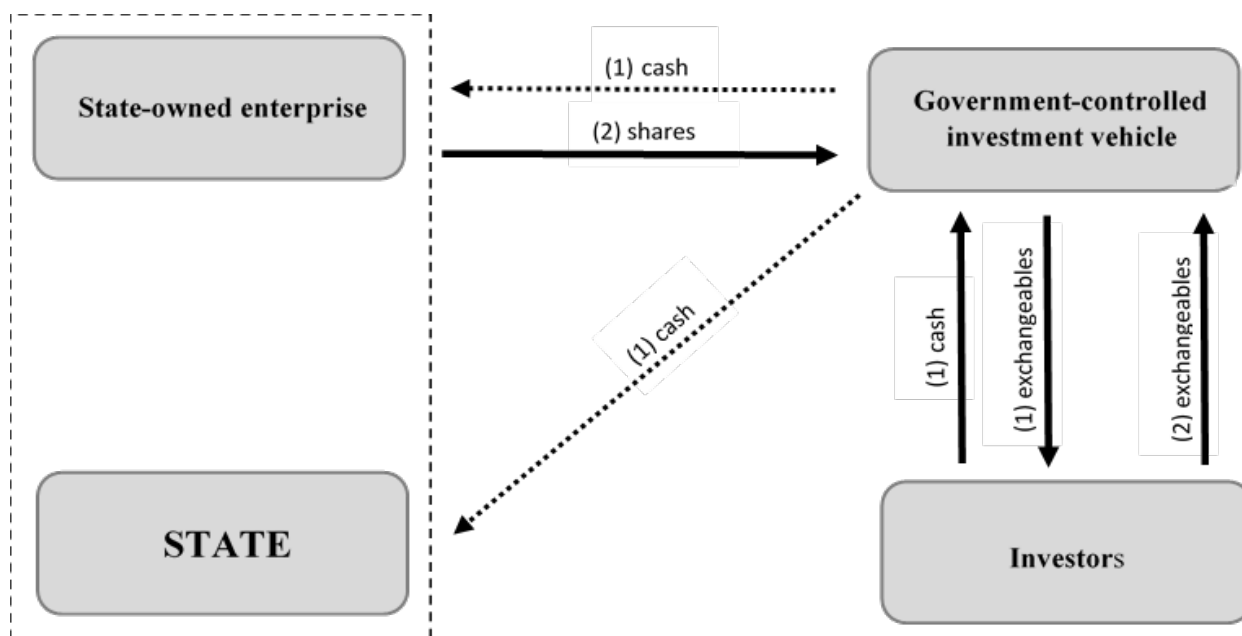


Figure 1. Privatization process with the use of exchangeable bonds

Source: own elaboration.

Data collection, sample selection, and methodology

A unique database was compiled of all identified issues of exchangeable bonds utilized in privatizations since the beginning of the 2000s. It was done manually using companies' annual reports, market disclosures, and press releases. The study concentrates on exchangeable issues conducted only through government-controlled investment vehicles (or their subsidiaries). Any equity exits not related to privatization were not included in the sample. Attention was focused exclusively on exchangeable debt issues (i.e., exchangeable bonds, exchangeable notes, and exchangeable certificates). Therefore, any types of debt-equity swaps, sovereign bonds exchanged for ownership rights in SOEs, and convertibles issued by state-owned companies for their own equity, were excluded from the analysis. After implementing these restrictions, the final sample encompasses sixteen exchangeable issues carried out in the privatization of companies from seven countries that operate in seven different economic sectors.

The empirical research was divided into three parts. In part one, the geographical and sectoral characteristics of exchangeables issued during privatizations since the 2000s were analyzed. Part two focuses on the issuers of equity-linked securities in search of motives for issuing debt exchangeable for ownership in SOEs. Part three examines major features of exchangeable bond issues, including maturity, coupons, and conversion premiums, to find common features of exchangeables issued for privatization purposes.

Analysis, results, and discussion

Table 1 presents an overview of the global market of exchangeable bonds used in privatizations since the beginning of the 2000s. Sixteen series of exchangeable bonds were issued in four countries in Europe (Austria: 2; Germany: 5; Hungary: 3; and Portugal: 3) and three countries in Asia (Singapore, Malaysia, and Papua New Guinea) (Table 1, column 2).

Table 1. An overview of the global exchangeables market in privatizations since the 2000s

Issue date	Country	Privatized company	Economic sector	Amount in currency
2003	Austria	Voestalpine AG	Basic materials	245,200,000 EUR
2003	Austria	Telekom Austria AG	Telecommunication	325,000,000 EUR
2003	Germany	Deutsche Post AG	Industrials	1,150,000,000 EUR
2003	Germany	Deutsche Telekom AG	Telecommunication	5,000,000,000 EUR
2004	Hungary	Gedeon Richter Ltd.	Healthcare	639,000,000 EUR
2004	Singapore	Singapore Telecom. Ltd.	Telecommunication	1,250,000,000 USD
2005	Germany	Deutsche Post AG	Industrials	1,100,000,000 EUR
2005	Portugal	EDP SA	Utilities	572,800,000 EUR
2006	Malaysia	Telekom Malaysia Bhd	Telecommunication	750,000,000 USD
2007	Portugal	EDP SA	Utilities	1,015,150,000 EUR
2008	Germany	Deutsche Telekom AG	Telecommunication	3,300,000,000 EUR
2009	Germany	Deutsche Post AG	Industrials	750,000,000 EUR
2009	Hungary	Gedeon Richter Ltd.	Healthcare	833,300,000 EUR
2009	PNG*	Oil Search Ltd.	Energy	1,168,000,000 AUD
2010	Portugal	Galp Energia SA	Energy	885,650,000 EUR
2013	Hungary	Gedeon Richter Ltd.	Healthcare	903,800,000 EUR

* PNG – Papua New Guinea.

Source: own elaboration.

Telecommunication companies comprised the largest group of the ten SOEs privatized by means of exchangeable debt (Deutsche Telekom AG, Singapore Telecommunications Ltd., Telekom Austria AG, and Telekom Malaysia Bhd). Other firms operated in the following sectors: energy (Galp Energia SGPS SA and Oil Search Ltd.), basic material (Voestalpine AG), industrial (Deutsche Post AG), healthcare (Gedeon Richter Ltd.), and utilities (EDP SA) (Table 1, column 4).

The total value of exchangeable bonds issued since the 2000s amounted to nearly USD 25 billion (Table 1, column 5). This could be considered a modest contribution considering that the total value of privatization revenues reached USD 266 billion in 2016 (OECD 2019). Four-fifths of issues were attributed to Europe, all denominated in Euro. Asian firms opted mostly for US dollar issues. Only one issue was denominated in Australian dollars.

Table 2 summarizes all exchangeable bond issuers from the research sample. Almost half of exchangeables were issued by state agencies involved in public asset management or privatization programs (i.e., the Hungarian National Asset Management (MNV) and its predecessor, the Hungarian Privatization and State Holding Company (APV), both in Hungary; Parpública in Portugal; the Independent Public Business Corporation (IPBC) in Papua New Guinea, and the Austrian Industrial Administration Limited-Liability Company (ÖIAG) in Austria). The second group of issuers constitutes investment agencies and sovereign wealth funds (or their subsidiaries), and special purpose entities (i.e., Temasek Holdings in Singapore and Khazanah Nasional in Malaysia). Finally, one issue was carried out by a development bank (i.e., Kreditanstalt für Wiederaufbau, KfW in Germany).

Table 2. The issuers of exchangeable bonds for privatization purposes since the 2000s

Issuer		Privatized company
APV/MNV* (Hungary)	Privatization agency/national asset management agency	Gedeon Richter
IPBC (Papua New Guinea)	Sovereign wealth fund	Oil Search
KfW (Germany)	Development bank	Deutsche Post, Deutsche Telekom
Khazanah Nasional** (Malaysia)	Sovereign wealth fund	Telekom Malaysia
ÖIAG (Austria)	Privatization agency	Telekom Austria, Voestalpine
Parpública (Portugal)	National asset management agency	EDP, Galp Energia
Temasek Holdings (Singapore)	Investment Agency	Singapore Telecommunications

* MNV is the successor of APV; ** Khazanah Nasional carried out the privatization of Telekom Malaysia through its SPV – Rafflesia Capital.

Source: own elaboration.

In-depth analysis shows that almost all exchangeable bonds were sold to international and institutional investors that operate in domestic markets (such as investment companies, banks, asset managers, insurance companies, and pension funds). They were then listed on stock exchanges (in Luxembourg, Frankfurt, Lisbon, Singapore, and Hong Kong). Only one issue was taken up by an industry investor to raise capital for investment purposes of the state.⁴ A few issues were aimed at retail investors outside the domestic market.⁵ Finally, private investors (i.e., current employees) subscribed to one issue to keep the shareholder structure due to the strategic importance of the privatized SOE for the state.⁶

The diversity of strategies applied by governments makes it possible to identify possible motives behind the issuance of exchangeable debt in the privatization of state-owned companies. Most exchangeable bond issues carried out for privatizations were highly innovative for the local capital markets. For instance, the Austrian ÖIAG placed the first exchangeable debt issuance in the Austrian market. The German KfW, issued in 2005, was the first foreign currency exchangeable bond offered by a non-Japanese issuer to Japanese household investors (commonly called Uridashi bonds). In 2006, Malaysia's Khazanah Nasional prepared the first offering of Shariah-compliant exchangeable debt in the world (exchangeable sukuk). These examples may indicate that the decision to issue exchangeable bonds was made with great deliberation, taking into account a variety of circumstances, including market conditions and periods of increased demand for high-quality credit in combination with very liquid underlying shares (which makes it possible to obtain attractive pricing of debt instruments used in such situations). Therefore, the issuance of exchangeables can perfectly complement the entire privatization process in addition to IPO, SPO, or block sales. From this point of view and after reviewing the terms and conditions of exchangeable issues presented in Table 3, four main rationales for the use of exchangeable debt can be distinguished.

Table 3. Terms of issue of exchangeable bonds issued for privatization purposes since the 2000s

Privatized company	Maturity (years)	Coupon (%)	Conversion premium (%)
Deutsche Post (2003)	4	0.500	30.0
Deutsche Post (2005)	4	0.500	12.0
Deutsche Post (2009)	5	1.500	35.0
Deutsche Telekom (2003)	5	0.750	38.0
Deutsche Telekom (2008)	5	3.250	27.5

⁴ Papua New Guinea, where exchangeables issued by IPBC were subscribed by the International Petroleum Investment Company of Abu Dhabi (IPIC).

⁵ Such as the exchangeables issued by KfW in Japan in 2005.

⁶ See the privatization of voestalpine AG in Austria in 2003.

Privatized company	Maturity (years)	Coupon (%)	Conversion premium (%)
EDP (2005)	5	2.690	43.0
EDP (2007)	7	3.250	45.0
Galp Energia (2010)	7	5.250	25.0
Gedeon Richter (2004)	5	1.000	54.0
Gedeon Richter (2009)	5	4.400	32.0
Gedeon Richter (2013)	5.5	3.375	35.0
Oil Search (2009)	5	5.000	72.4
Singapore Telecom.(2004)	5	0.000	4.8
Telekom Austria (2003)	3	1.125	35.0
Telekom Malaysia (2006)	5	1.250	19.0
Voestalpine (2003)	3	1.500	27.0
Mean	5	2.2	33.4

Source: own elaboration.

First, the issuance of exchangeables enables the issuing company to get a higher price for the shares sold as a result of debt conversion. Thus, they are commonly used when privatized entities are severely undervalued⁷ or during high volatility of stock markets due to uncertainty.⁸ This is a probable reason why the average premium for the sample of exchangeables exceeds 30%. It represents the upper limit of an average conversion premium for convertible debt estimated from 20 to 30% (Das 2003). What is more, to assure a relatively high price for common stock, issuers often give bondholders the right to convert exchangeables into SOE equity only in the last years before maturity.⁹ To maintain balance, they often add a call option that allows the early redemption of bonds with no obligation to convert them into equity if privatization ultimately becomes undesirable. Sometimes they even offer cash in exchange for giving up conversion.¹⁰

Second, issuers may use exchangeable bonds due to privatization plans that assume a careful and gradual exit from the privatized entities without causing a drop in their share price following the sale of a large block of shares to external investors.¹¹ This argument is supported by the outcomes that indicate that underlying shares that exchange-

⁷ Exemplified by the privatization of the state postal and telecommunication services in Austria and Germany in 2003.

⁸ See for reference the privatizations of EDP and Galp Energia in Portugal.

⁹ For example, the privatization of the EDP in 2005 in Portugal.

¹⁰ As with the privatization of Gedeon Richter in Hungary in 2013.

¹¹ Illustrated by the privatization of Gedeon Richter in 2004 in Hungary and Telekom Malaysia Bhd. in Malaysia in 2006.

able bonds can be converted into constitute nearly 6% of the outstanding share capital of the privatized companies.

Third, the issuance of exchangeable bonds may be perceived by issuers as relatively cheap and long-term external capital which can directly supply state budgets,¹² fund state investment projects,¹³ or finance the principal business of the issuing companies.¹⁴ These observations are supported by an average maturity of sample exchangeables of five years and an average coupon equal to 2.2% (median: 1.5%). This is approximately twice as low as the average government bond interest rate in corresponding years. The difference is most pronounced in Germany (3.0–4.0% for 10Y government bond yields vs. 0.5–3.0% for exchangeables), Austria (approx. 4.0% vs. 1.0–1.5%), Hungary (6.0–9.0% vs. 1.0–4.5%), and Portugal (3.5–5.5% vs. 2.5–5.0%).

Fourth, by issuing exchangeables, the issuers can keep all dividends from privatized subsidiaries until conversion and maintain a real impact on their operational activity. However, confirmation of this thesis requires further in-depth qualitative research.

Finally, every third exchangeable issue from the sample (amounting to approx. USD 10 billion) was carried out to refinance maturing bonds that had not been converted into shares in the privatized companies. There are many indications that, in some cases, issuers did not even want the issue to end in conversion. Their main intention was to remain a shareholder in privatized SOEs and continue to exercise their ownership rights in accordance with state economic interests.¹⁵

Following the results of the research, the effects of privatizing SOEs through exchangeable bonds cannot be assessed unambiguously. First of all, more than half of the issues from the sample did not result in the conversion of debt into equity, which seemed to be the primary aim of the issuers in the majority of cases¹⁶. The conversion failure was mainly caused by unfavorable market conditions, which effectively discouraged bondholders from exchanging bonds for shares of privatized entities.¹⁷ On the other hand, the complete success of the privatization strategies based on hybrid debt can be seen in Austria, Papua New Guinea, and Germany¹⁸. Hence, further in-depth research in this area is necessary.

12 Resembling the privatized companies in Germany and Portugal.

13 As in Papua New Guinea.

14 As in Malaysia or Singapore.

15 For example, the privatization of Gedeon Richter in 2009 and 2013.

16 For example, Deutsche Telekom AG and Galp Energia SA.

17 See the privatization of EDP SA.

18 Privatizations of, consecutively, voestalpine AG, Telekom Austria AG, Oil Search Ltd. and Deutsche Post AG.

The issuance of exchangeable bonds for the privatization of SOEs was previously discussed in Russia. Such a plan was considered for the privatization of VTB Bank in 2002–2003 (they were going to be five-year bonds exchanged for 10–20% of VTB's shares), but it ultimately ended up with an ordinary sale of shares in the financial market. The idea of issuing exchangeable bonds was then revisited in 2011–2013 for the privatization of Alrosa and Sberbank, but this ended in fiasco again (Pronina 2011). The issuance of hybrid debt instruments for the privatization of state-owned enterprises was also considered in Poland by the Treasury Ministry in 2007–2009 (Bujnicki 2017) and 2012 (Zatoński 2012). However, despite initial plans, their widespread use in the Polish financial market has not occurred.

Conclusions

The issuance of bonds that are exchangeable for shares in state-owned enterprises carried out via government-controlled investment vehicles is a privatization method that is used in different parts of the world. However, this topic has hardly been addressed in previous research. Therefore, the purpose of this article was to fill the research gap and contribute to the literature with new research insights into the little-known mechanism for using exchangeable bonds during privatization via financial markets. Using a unique research sample that comprised sixteen exchangeable issues carried out in seven countries since the 2000s, the article identified key motives for the issuance of exchangeable debt in the privatization of SOEs through dedicated state entities. It also explained why states use hybrid debt instruments as a more favorable alternative to traditional ways of disposing of state ownership, such as IPOs, SPOs or trade sales. The main conclusions to be drawn from this article are as follows.

First, the total value of exchangeable bonds issued for privatization purposes since the 2000s, which amounts to almost USD 25 billion, very strongly contrasts with the more than USD 250 billion of total privatization revenues earned only in 2016, according to the latest OECD data. More specifically, over the last twenty years, sixteen series of exchangeables were issued to privatize ten SOEs in Europe and Asia (i.e., Austria, Germany, Hungary, Portugal, Singapore, Malaysia, and Papua New Guinea) that operate in various sectors from telecommunication and energy to basic materials, industrials, healthcare, and utilities (i.e., Austria Telekom, voestalpine, Deutsche Telekom, Deutsche Post, Gedeon Richter, Galp Energia SGPS, EDP, Singapore Telecommunications, Telekom Malaysia, and Oil Search).

Second, government-controlled investment vehicles that intermediated in the privatization of SOEs through exchangeable debt included state agencies involved in privatization programs, investment agencies, sovereign wealth funds, and development banks (i.e., MNV in Hungary, Parública in Portugal, IPBC in Papua New Guinea, ÖIAG in Austria, Temasek Holdings in Singapore, Khazanah Nasional in Malaysia, and KfW in Germany).

Third, most exchangeable issues were highly innovative for the local capital markets (e.g., the first Shariah-compliant exchangeable debt issued in Malaysia or the first exchangeable debt issuance in Austria). Moreover, many of them were then listed on major world exchanges (i.e., in Luxembourg, Frankfurt, Lisbon, Singapore, and Hong Kong). Exchangeables were mostly sold to domestic and international institutional investors (such as investment companies, banks, asset managers, insurance companies, and pension funds). Only a few were aimed at retail investors in or outside a domestic market.

Lastly, the analysis indicates that in some cases, selling SOE shares through exchangeable bonds can be more beneficial for the stakeholders than disposing of them directly on the capital market through IPOs, SPOs or trade sales. Such situations may include, among others, periods when privatized companies are severely undervalued or there is high volatility in stock markets due to extraordinary uncertainty. This presumption has been initially confirmed by the observations that by using exchangeable bonds: (1) Shares may be sold at a higher price (due to a 30–50% conversion premium embedded in the analyzed exchangeables); (2) The impact on the stock market price of the privatized company may be less disruptive to shareholders (the underlying shares into which exchangeable bonds can be converted constitute a modest portion of outstanding share capital); (3) The entire privatization process tends to be more flexible (the state keeps control over the privatized company, receives all dividends paid until conversion of hybrid debt, and can cease the privatization at any time by exercising a call option attached to exchangeables); and (4) The issuance of exchangeable bonds constitutes a relatively cheap and long-term external capital for the issuers, which can finance their business or contribute to the state budget (an average coupon of exchangeables is twice as low as the average government bond yields in corresponding years).

The findings of this paper relate to research in corporate finance examining the motives that drive hybrid debt issues. The article is perhaps the first to provide a comprehensive analysis of using exchangeable bonds for privatization and lays the groundwork for further research on equity-linked securities in the privatization of SOEs. Looking forward, it would first be useful to examine whether the decision to issue exchangeable bonds is related to periods when privatized companies are severely undervalued, and there are extraordinary fluctuations in the stock market. This would demonstrate whether exchangeable bonds are considered the most appropriate instrument for privatization in specific market conditions. Consequently, it would then be necessary to investigate how the SOE share price fluctuates in the short, medium and long terms after the announcement of an exchangeables issue for shares of the privatized company. This would answer how investors view the use of hybrid bonds for privatizations (i.e., whether they provide positive or negative information about a privatized company).

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Motywy emisji obligacji wymiennych w procesach prywatyzacyjnych przedsiębiorstw państwowych

Na podstawie unikalnej próby obligacji wymiennych wyemitowanych w siedmiu krajach w XXI wieku w artykule przeanalizowano rolę hybrydowych instrumentów dłużnych w procesach prywatyzacyjnych przedsiębiorstw państwowych. Z przeprowadzonego badania wynika, że dotychczas wyemitowano szesnaście serii obligacji wymiennych o łącznej wartości ok. 25 mld USD w celu prywatyzacji dziesięciu przedsiębiorstw w Europie i Azji, działających w sektorach: telekomunikacyjnym, energetycznym, materiałów podstawowych, przemysłowym, opieki zdrowotnej i użyteczności publicznej. Ponadto wykorzystanie obligacji wymiennych w celu prywatyzacji przedsiębiorstw państwowych może w niektórych przypadkach stanowić korzystniejszą alternatywę dla tradycyjnej oferty sprzedaży akcji prywatyzowanych spółek na rynku kapitałowym (np. w okresach niedowartościowania akcji lub dużych wahań indeksów giełdowych). Po pierwsze, emitenci mogą dokonać sprzedaży akcji prywatyzowanych przedsiębiorstw w późniejszym czasie i po wyższej cenie. Po drugie, emisja obligacji wymiennych może mieć mniej negatywny wpływ na notowania giełdowe prywatyzowanej spółki. Po trzecie, proces prywatyzacji może być postrzegany jako bardziej elastyczny przez samych emitentów, ponieważ mogą oni wykorzystywać środki z emisji długu hybrydowego jako źródło tańszego i długoterminowego kapitału zewnętrznego oraz zachowywać kontrolę nad prywatyzowaną spółką do czasu ewentualnej konwersji obligacji przez obligatariuszy.

Słowa kluczowe: przedsiębiorstwa państwowe, prywatyzacja, hybrydowe instrumenty dłużne, obligacje wymienne