

Nunnenkamp, Peter

Book Review — Digitized Version

[Book Review of] State investment companies in Western Europe. Picking winners or backing losers? London, 1983

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Hindley, Brian (Ed.), *State Investment Companies in Western Europe. Picking Winners or Backing Losers?* London 1983. The Macmillan Press Ltd. for the Trade Policy Research Centre. XXIV, 293 pp.

In the recent past all kinds of economic activity by governments have become subject to harsh attacks. The ability of policymakers to improve the overall economic performance by indirectly interfering in the market mechanism via discretionary fiscal and monetary measures is widely questioned. Public enterprises as a direct way to control important segments of the economies are under scrutiny, since the theory of government failure has told us that this may result in technical and allocative inefficiency and impede structural change. The volume edited by Hindley adds to this scepticism by focussing on a so far neglected area of economic policy, i.e. state investment companies.

State investment companies constitute an important element of industrial policy in many Western European countries and frequently imply a "back-door nationalisation". Especially in the late 1960s they gained considerably in importance. In an introductory chapter, the editor discusses the case for these companies and presents three major functions supporters expect them to perform. First of all, state investment companies are established to provide public funds for profitable investment opportunities that are neglected by private investors. Other forms of market failure state investment companies are considered to correct may be seen in an insufficient supply of particular types of finance (e.g. equity capital or long-term credits) and a shortage of funds for particular classes of companies (e.g. small enterprises or businesses located in specific regions). An important field of state investment companies' activities is centered around the rescue of companies that would fail without infusions of public funds. The principal argument is to maintain employment by securing jobs in troubled private enterprises. Finally, they are thought to act as a buffer between governments and public enterprises. This may serve two purposes: reducing political pressures and providing business expertise.

A lot of well-known arguments give rise to severe doubts as to whether state investment companies can actually succeed in these respects. Hindley summarizes the theoretical discussion and convincingly refutes some everlasting reasonings. Why is it, for example, that public managers or even bureaucrats should know better than private entrepreneurs which investments will prove to be profitable and which will fail (see the example of a former West German Minister of the Treasury cited by Jüttemeier and Schatz on p. 256)? Frequently, assumed market failures rather result from government failure, as in the Belgian case (presented by de Grauwe and van de Velde) where the lack of equity capital stems from the preferential tax and subsidy treatment of debt financing. Maintaining jobs in businesses that are no longer competitive without official capital provisions and other forms of protection may severely impede the competitiveness of those enterprises that have to pay for public assistance. Consequently, overall employment is likely to be negatively affected.

This rather grim picture based on a priori considerations notwithstanding, Hindley is correct in stating that at bottom it is an empirical question whether state investment companies will be able to fulfill their perceived purposes. This is why the Trade Policy Research Centre embarked on the programme of studies published in this volume. Included are seven country-specific papers dealing with Italy (Pontarollo), the Netherlands (de Jong, Spierenburg), Belgium (de Grauwe, van de Velde), the

United Kingdom (two papers by Hindley, Richardson), Sweden (Eliasson, Ysander), France (Green) and West Germany (Jüttemeier, Schatz). Apparently, the Trade Policy Research Centre succeeded in forming a group of highly expertised economists who know their countries' experiences with state investment companies extremely well. The reader interested in the historical background of establishing state investment companies, their particular roles and objectives as well as the specific instruments applied and their consequences will greatly benefit from this collection of papers.

Most papers included in this volume remain largely descriptive rather than presenting analytical research, however. As mentioned by several authors (see e.g. pp. 138–139, 187, 211–212, 216, 271), the performance of state investment companies is difficult to assess quantitatively. This is partly due to the extremely vague and complex objectives these companies are expected to fulfill. Additionally, some uneasiness remains with respect to the avenue followed in most of the papers, namely to compare the profitability of businesses sponsored by state investment companies on the one hand and investments without official support on the other. This is because the supporters of the provision of public funds will argue that it is social efficiency rather than microeconomic profitability that state investment companies should strive for. Thus it remains highly dubious that those in favour of these companies will be impressed by the editor of concluding: "The papers collected in this volume give no grounds to suppose that the operation of any economy has been improved by a state investment company" (p. 23). Perhaps this issue could have been dealt with more controversially if the Trade Policy Research Centre would have invited discussants to the country papers who are known to be less sceptical about state intervention.

The qualifications from above should not be misunderstood, however. The central claim of most state investment companies says that they will be able of picking winners that were neglected by the private sector. In some instances, it is explicitly stated that profitability is a necessary part of success (see e.g. pp. 139 and 178). At least in these cases the comparison of profitability is highly relevant. The evidence presented in most of the country papers sharply contradicts the hypothesis of picking winners. Moreover, comparing profit performance gives an indication of the financial burden going along with the alleged social benefits of the state investment companies' activities. Finally, it should be noted that positive social effects cannot be relied upon. The paper by de Jong and Spierenburg on the Netherlands, for example, concludes that as regards employment objectives the operation of the state investment bank proved to be a failure.

What are the lessons to be learnt? Most of the authors abstain from drawing comprehensive and far-reaching conclusions. Mainly Eliasson and Ysander consider alternatives to state investment companies as a means to fulfill social objectives. Technical difficulties of implementation notwithstanding, their suggestion of a bidding mechanism for a minimum cost solution to social adjustment problems is most interesting. On the other hand, some papers come up with rather confusing and highly ambiguous conclusions. For the Netherlands, for example, it is stated that industrial policy "is in need of total remodelling, if not total abolition" (p. 90). Is this meant as admitting that the analysis has not helped to settle the question whether state investment companies can play a promising role or not?

Peter Nunnenkamp