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The PB Newsletter

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Reporting on privatization in the enlarged Europe

It's the Politics, Stupid!

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THE WEBSITE ON PRIVATIZATION IN EUROPE

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What is the PB Newsletter?

The PB Newsletter is a semi-annual report on privatization activity in the enlarged European Union. It aims at monitoring the most recent trends, at analyzing aggregate data on revenues and transactions, and at providing updated statistics at the country and sector level.

The PB Newsletter highlights the most important deals, which are regularly commented on by privatization guru William L. Megginson. It also hosts contributed articles by top international scholars, who will make accessible to the reader the most recent results of professional research.

The Newsletter also report on the PB indexes, a series of indicators which follow the performance of equity investment in privatized companies in the EU.

Rigorous, updated, easily accessible and freely distributed on the web, the PB Newsletter is an authoritative source of information and a vehicle for a more informed discussion on the choices and consequences of privatization.

Italian Version

Su scala globale, i governi del mondo hanno accelerato significativamente i processi di privatizzazione nel corso del 2006, ma questo non è accaduto in Europa. Con 62 operazioni per un controvalore di 41 miliardi di euro, il bilancio delle privatizzazioni europee non è affatto trascurabile, ma comunque segna un forte ribasso rispetto ai 67 miliardi di euro del 2005.

Il record del 2005 - il più alto valore dall'inizio del secolo - è un fatto eccezionale. Un esame attento delle tendenze in atto suggerisce che le privatizzazioni europee hanno probabilmente raggiunto un'area di resistenza riferibile all'attuale contesto politico ed economico. In importanti paesi membri la politica si è spostata a sinistra e alcuni tra i più grandi paesi della Nuova Europa, in particolare la Polonia, hanno accantonato le riforme strutturali per riprendere la via del protezionismo. Questo nuovo contesto politico ha certamente contribuito al rallentamento nei processi di apertura dei mercati e di privatizzazione.

Non a caso il grande assente del 2006 è proprio l'Italia, uno dei motori del processo di privatizzazione su scala globale. Il bilancio italiano del 2006, pari a solo 700 milioni di euro, è molto modesto e fa retrocedere il paese in dodicesima posizione nella classifica europea. Nessuna operazione è stata portata a termine da quando si è insediato il nuovo governo, che è comunque attualmente impegnato nella difficile vendita di Alitalia. La sfida sarà trasformare le iniziali manifestazioni di interesse in offerte concrete.

Un altro fatto importante che documentiamo nel 2006 è la maggiore rilevanza delle privatizzazioni in comparti concorrenziali quali il manifatturiero e finanziario e il rallentamento nelle industrie di rete e in particolare nelle *utilities*. Se da un lato il consolidamento del settore bancario sta facendo notevoli progressi, dall'altro il settore energetico appare statico, probabilmente come riflesso di un acceso dibattito che sta coinvolgendo i vertici dell'economia della politica europea. La Francia e la Germania hanno criticato la proposta di riforme strutturali predisposte dalla Commissione Europea in materia di energia, e questa tensione ha originato tendenze protezionistiche che hanno influito negativamente sulle vendite.

Mentre questa battaglia è in corso, un nuovo tipo di investitore sta salendo alla ribalta: i fondi di private equity. Secondo stime recenti, più di 2,700 fondi sono oggi operativi con un potere d'acquisto complessivo di circa 2,000 miliardi di euro e diversi governi europei hanno scoperto che tali fondi sono da tenere in seria considerazione anche nelle operazioni di maggiori dimensioni. Le scelte sui metodi di vendita riflettono queste nuove tendenze. Circa il 66 percento dei proventi dell'anno sono stati raccolti tramite collocamenti diretti, e il 40 percento di questi ultimi è stato realizzato grazie a fondi di private equity. Le implicazioni di questo processo cominciano ad emergere soprattutto perché le quote rilevanti che tali fondi acquisiscono permettono di esercitare un'influenza significativa sulla corporate governance delle società privatizzate. Ma veramente i fondi di private equity saranno i nuovi protagonisti delle privatizzazioni future su scala globale? Andrea Levantini di Morgan Stanley affronta la questione dalla prospettiva del banchiere.

Levantini sottolinea che in passato i fondi di private equity non hanno partecipato al processo di privatizzazione per una serie di motivi che vanno da un generico scetticismo dei governi nei confronti di questa categoria di investitori ai vincoli di natura regolatoria che spesso vengono imposti in queste operazioni. Questa diffidenza sta rapidamente scomparendo. Oggi i governi sono più propensi ad accettare i loro metodi operativi poiché si rendono conto che possono apportare importanti benefici nel management delle privatizzate. Sfruttando il gap informativo tra management e mercato, il private equity è in grado di ristrutturare profondamente le società e incentivare meglio il consiglio di amministrazione. La recente acquisizione da parte di Blackstone - uno dei principali fondi americani – di una partecipazione importante di Deutsche Telekom rappresenta un caso interessante di attivismo degli investitori, e rispecchia una tendenza in atto anche nelle imprese private in cui iniziative simili sono state promosse dai più importanti hedge funds.

Al di là dell'ambito strettamente Europeo, il sistema finanziario cinese sta vivendo delle trasformazioni davvero impressionanti. Il Privatization Barometer mostra anche in questa Newsletter il suo impegno a seguirlo da vicino. Il professor Lihui Tian, dell'Università di Pechino, ci fornisce una panoramica sulle più recenti evoluzioni del sistema bancario cinese. L'evento chiave dell'anno è sicuramente rappresentato dall'IPO di Industrial and Commercial Bank of China, la più grande della storia, che ha avuto un grande successo, tuttavia non mancano i problemi. Infatti, il gigantesco mercato è potenzialmente profittevole, ma ancora fortemente penalizzato dal problema delle sofferenze bancarie. La quotazione delle grandi banche (le cosiddette Big Four) sui mercati internazionali ha di certo contribuito a migliorarne la corporate governance, ma una vera trasformazione del sistema sarà soltanto possibile quando il governo cinese deciderà davvero di rispettare le regole del mercato.

Le previsioni di PB riguardo all'anno appena concluso si sono dimostrate precise. Il ribasso era stato correttamente anticipato e il bilancio si è chiuso in linea con le aspettative. Per quanto riguarda il 2007, riteniamo che le privatizzazioni abbiano raggiunto una resistenza e che il controvalore finale non sarà quindi inferiore ai 40 miliardi di euro. La locomotiva tedesca continuerà il suo percorso, la Svezia comincerà a fare sul serio, mentre l'incertezza politica dominerà la scena in Francia. Ma la questione più importante è se e quando il processo riprenderà nei settori strategici. La risposta dipenderà dalle scelte future della politica europea.

English Version

Governments around the world pushed strongly the privatization agenda throughout 2006. However, this did not happen in Europe. With 62 deals worth €41 billion, the balance of privatization activity in the enlarged European Union is far from negligible, but still marks a significant downward correction with respect to the €67 billion raised in 2005.

Indeed, 2005 record – the highest value since the turn of the century – was an exceptional year. Yet a careful examination of the current trends suggest that privatization flows in Europe have likely reached a plateau which can be traced back to the current economic and political environment. In some core European member states, the political pendulum shifted to the left and important countries of the New Europe, notably Poland, have apparently abandoned the road to economic reform and embraced economic protectionism. Indeed, this new political climate has contributed to a slowdown in market opening and privatization.

A reflection of this new trend is the revealing absence of Italy – traditionally one of the engines of the privatization process at the global scale - in the European rankings. Italy closes the 2006 balance in twelfth position with a modest €700 million. Importantly, no single operation has been executed since the new center-left government took office. The government is actually engaged in the controversial sale of Alitalia, the national air carrier, and turning the initial expressions of interest into serious bids will be a difficult challenge due to the political constraints that will likely be imposed on the sale contract.

Another important new fact that we document in 2006 is the rising share of privatization activity in more competitive sectors such as manufacturing and finance, as opposed to network industries, and especially utilities, which now account for a modest share of revenues. While the consolidation of the banking industry is advancing fast, we do not observe significant progress in the energy sector. The actual stalemate is partly explained by the debate which is taking place at the highest level in Europe. France and Germany have strongly opposed a radical reform package set forth recently by the European Commission, and this tension has created a protectionist backlash against cross-border takeover activity and further privatization.

While this battle is underway, a new type of investor is emerging as the most prominent player in privatization: private equity funds. According to recent accounts, more than 2,700 are currently active with an aggregate purchasing power of approximately €2 trillion. Several European governments have discovered this year that these investors represent an interesting set of buyers even for large holdings. As a consequence, we find that 66 percent of total yearly revenues have been raised by direct placements, of which 40 percent by private equity funds. The implications of the rise of private equity funds are becoming visible, especially because the large stakes they acquire allow them to exert significant influence in the corporate governance of privatized firms. But will private equity become truly pivotal in the global privatization process? Andrea Levantini from Morgan Stanley provides us with the investment banker's point of view on this important issue.

Levantini points out that in the past private equity funds did not actively participate in privatizations due to a combination of factors, ranging from a generic governmental skepticism towards this type of investor to the regulatory constraints imposed in many privatizations. Yet this attitude is changing rapidly. Today governments tend to accept more easily private equity investment methods because they realize that private equity funds may provide essentially a new model of management. By exploiting the large information gap between what managers know and what the public shareholders know, these funds can heavily restructure the companies or re-motivate the boards of directors. The recent acquisition by Blackstone – one of the largest funds in America - of a blockholding in Deutsche Telekom represents an interesting example of shareholder activism, mirroring what is currently happening in the private corporate world, where a similar activism has been brought in by the most important hedge and private equity funds.

Radical transformations are taking place in the Chinese financial system and the Privatization Barometer maintained its commitment to track closely this process. Professor Lihui Tian of Peking University provides an overview of the most recent evolution of the banking system in China. The recent floatation of the Industrial and Commercial Bank of China was one of the largest IPOs in history, and was extremely successful. Yet Chinese banks can be a honey pot or a plague. The Chinese market is huge and potentially lucrative, but still burdened by a huge amount of non performing loans. Overseas listing of these banks has strongly improved the corporate governance, but the successful transformation will depend upon the Chinese government's determination to respect the market rules.

PB forecasts have proved to be quite correct in the past. The decline in activity was anticipated and the 2006 balance is close to our expectation. In 2007 we expect that European privatization will reach a plateau and will not fall below €40 billion. Germany will certainly remain the privatization heavyweight. Sweden will make a fresh start by launching large scale divestiture, while political uncertainty will slow down the process in France. But the big question is whether the process will resume in strategic industries. The answer will rest on the future of European politics.

Bernardo Bortolotti

University of Turin and FEEM

Privatization Trends in Europe

Economic growth revamped in Europe during 2006…

A booming world economy finally reached Europe, which in 2006 left an extended period of sluggish growth behind. For the first time in six years, the Eurozone reported an upswing mainly driven by a rapid expansion of investment and final consumption expenditure. Employment also picked up, and the same happened in equity markets, which have grown steadily especially in the second semester.

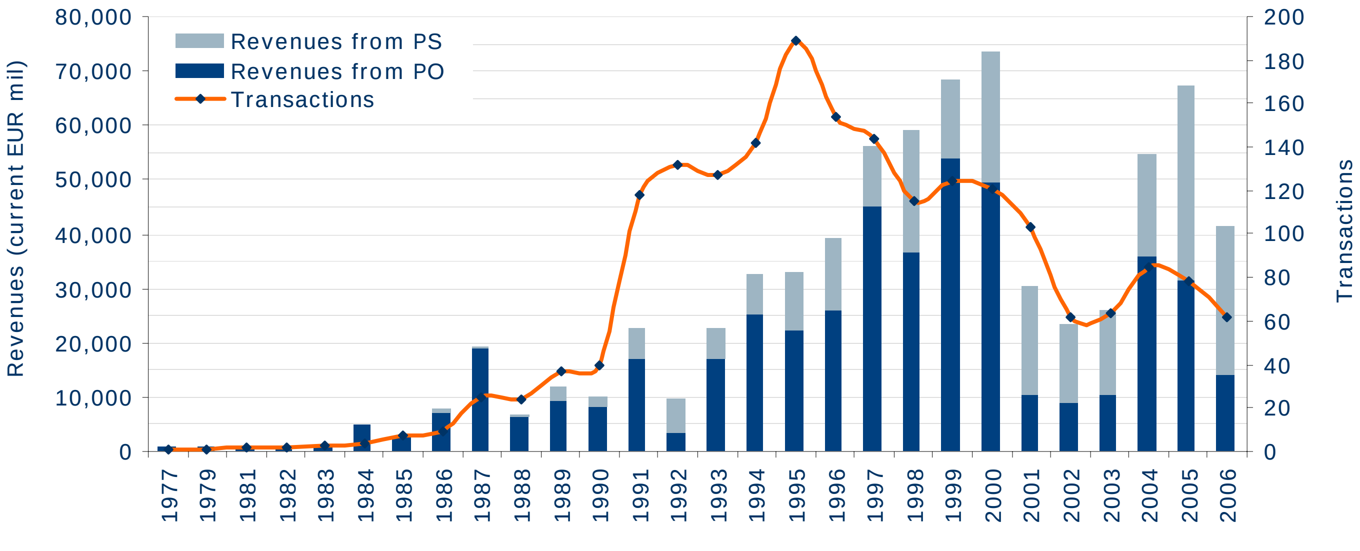
…but privatization activity did not catch up with 2005 record

In 2006, Europe did not take advantage of this positive outlook on the macroeconomic front to accelerate the privatization agenda. Rather, after the 2005 binge, divesting governments sobered up in 2006. With 62 deals worth approximately €41.19 billion and conducted in 20 countries, the balance of privatization activity in the enlarged European Union is still significant but also marks a significant downward correction versus the €67.7 billion total of 2005, the highest value since the turn of the century.

The recent and worldwide political shift to the left is mirrored in less pro-market policies

Such a correction was largely expected and quite easily explained. Globalization discontents hit by the fall in real wages have pushed for social protection and caused a fundamental change in the political alignment in the industrial world, with several countries shifting from pro-capital right to the pro-labor left governments. In Europe, this trend is clearly visible in Italy after the victory of the center-left coalition led by Romano Prodi, in Germany where Angela Merkel's policies tilted towards labor after almost losing on a pro-market electoral platform, and also in France with the rising popularity of the socialist Ségolène Royal at the forthcoming presidential elections. Around the world, this tendency manifested in the US after mid-term elections, in Japan and in Australia. This new

Figure 1. Privatization in the Enlarged Europe: Total Revenues and Transactions 1977 - 2006



Source: *Privatization Barometer*

political environment has heightened the risk of a protectionist backlash, as opposed to market opening and privatization. Indeed, with the political pendulum swinging to the left, it is not surprising to see more state involvement in economic activity, rather than its retreat.

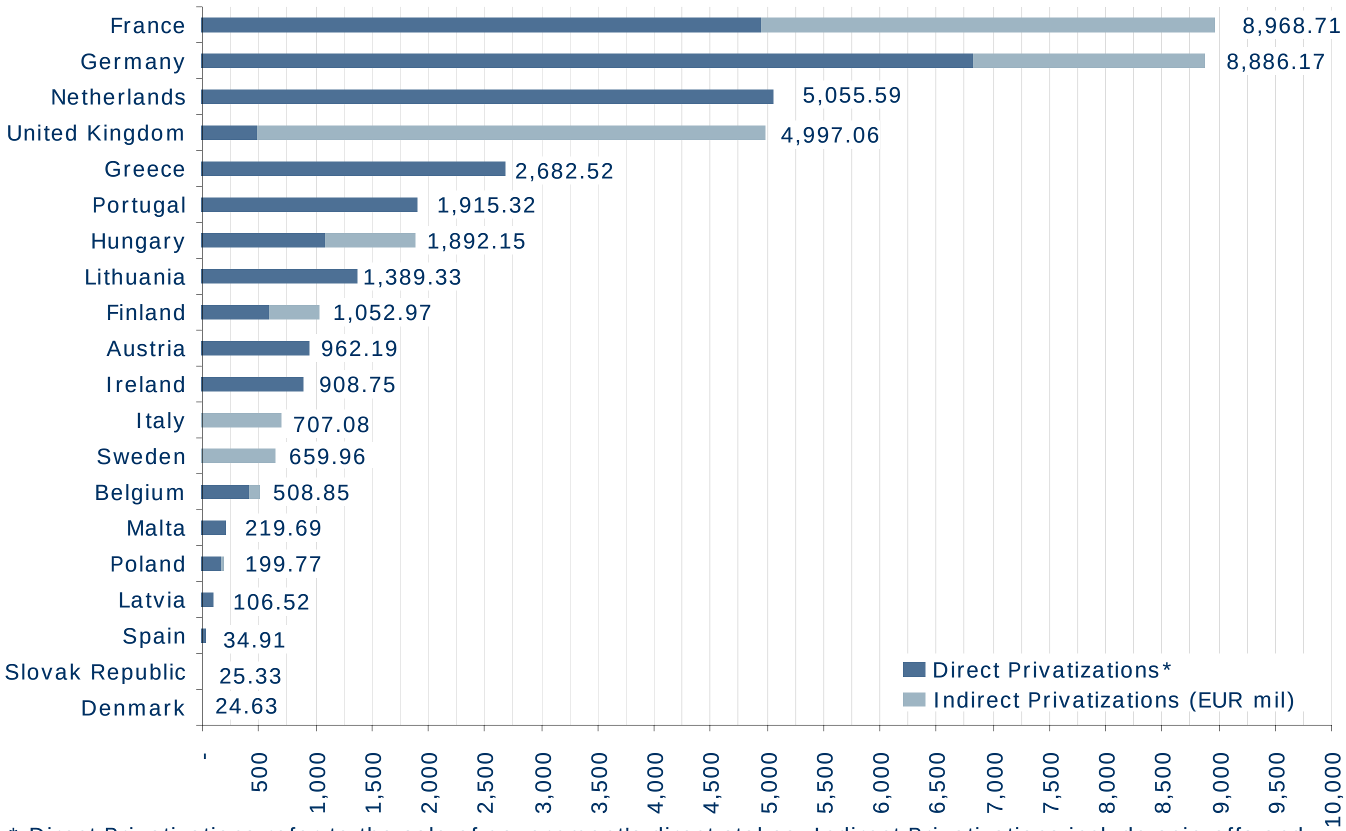
Against this background, the most interesting facts that we document for 2006 are (i) the absence of Italy; (ii) the predominance of sales in non strategic sectors; and (iii) the rise of private equity funds.

A privatization heavyweight missing: Italy

Italy has been one of the engines of the privatization process at the global scale and played a major role in the resumption of the process after the end-of-century plunge. With US$158 billion (€140 billion) raised since 1985, Italy ranks second in the global ranking by total privatization revenues. Italy closes 2006 with a modest balance of €700 millions largely due to a handful of sales in the first semester, notably the IPO of Ansaldo STS, the transport technology group. Importantly, no single sale is reported since the new government took office. As is widely known, the Minister of the Economy and Finance is actually engaged in the controversial sale of the financially distressed air carrier Alitalia. Some potential investors have shown up, and turning these initial expressions of interest into real bids will be a real challenge for the divesting government. This sale is likely to see the light in 1H2007.

Yet on the basis of official documents and announcements, no significant progress is expected for the near future on the privatization front. This is certainly not due to lack of inventory of assets. According to our estimates, central and local government ownership in listed companies is worth around €63 billion, and unlisted non-financial assets in State hands are valued almost €182 billion.

Figure 2. Distribution of Privatization Revenues by Country, 2006



* Direct Privatizations refer to the sale of government's direct stakes. Indirect Privatizations include spin-offs and transfer of shares from government owned companies.
Source: *Privatization Barometer*

Stalemate in network industries and strategic sectors…

The data on the distribution of revenues by industry document that privatizations in 2006 have been primarily conducted in competitive sectors, rather than network industries. The financial and manufacturing sectors accounted for almost a half of total revenues, while strategic sectors such energy and utilities are lagging behind gathering together a bare 13 percent.

...progress in banking and postal services

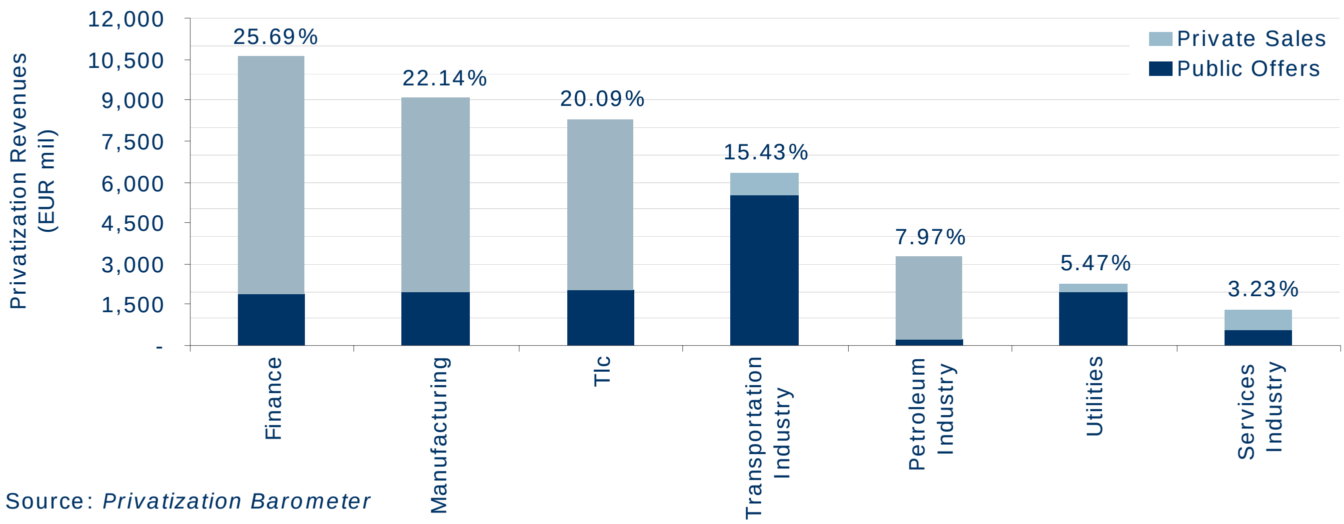
The consolidation of the European banking sector is advancing fast, and divestiture of banking assets has been a driver of this process. Bank privatizations during 2H2006 raised €8 billion, mostly due to the majority stake acquired by Crédit Agricole in the Greek Emporiki Bank and to significant transactions in two regional German banks--HSH Nordbank and Landesbank Berlin Holding. Within network industries, we report substantial activity in the transportation sector largely due to the contribution of sales in the postal services mainly executed in 2H2006. The contribution of these privatizations is quite impressive. Divestiture of postal assets by the Belgian, French, German, and Dutch governments totaled €3.7 billion, almost 60 percent of the sector total. Thanks to the recent privatization wave, the roll back of the state in the ownership of postal assets has been remarkable. As of end 2006, the Dutch Koninklijke TNT is a fully privatized company; in Belgium and Germany the central government is no longer the majority owner of postal operators, which are now exposed to some degree to competition and to the discipline of financial markets.

Utilities are locked in a political struggle on energy policy heightening the risk of protectionism

While some progress is made in some network industries, energy privatization is stalled. The only significant sale reported is the IPO of the Portuguese oil and gas operator, GalpEnergia. This stalemate certainly reflects the controversial debate on energy policy in Europe. France and Germany have joined forces to oppose a radical reform package recently set forth by the European Commission that strongly endorsed the ownership unbundling of supply from distribution network to promote competition and consumer welfare. The two governments declared that they would not accept a forced break up of their national champions (such as EdF, GdF, E.On and RWE) arguing that it would be detrimental to the security of energy supply, a politically sensitive issue which should be left to national policies.

The tension between these two core European member states (with others "hiding" behind) and the European Commission has been further exacerbated by a protectionist backlash against cross border takeover attempts on Suez Group by

Figure 3. Distribution of Privatization Revenues by Sector, 2006



Source: *Privatization Barometer*

Enel, and on Endesa by E.On. As we write, both cases have not been resolved yet, even if the last knockout bid by E.On will likely overcome the Spanish opposition. In any case, when the general attitude is raising barriers to protect national industries, it is difficult to see progress in genuine divestiture.

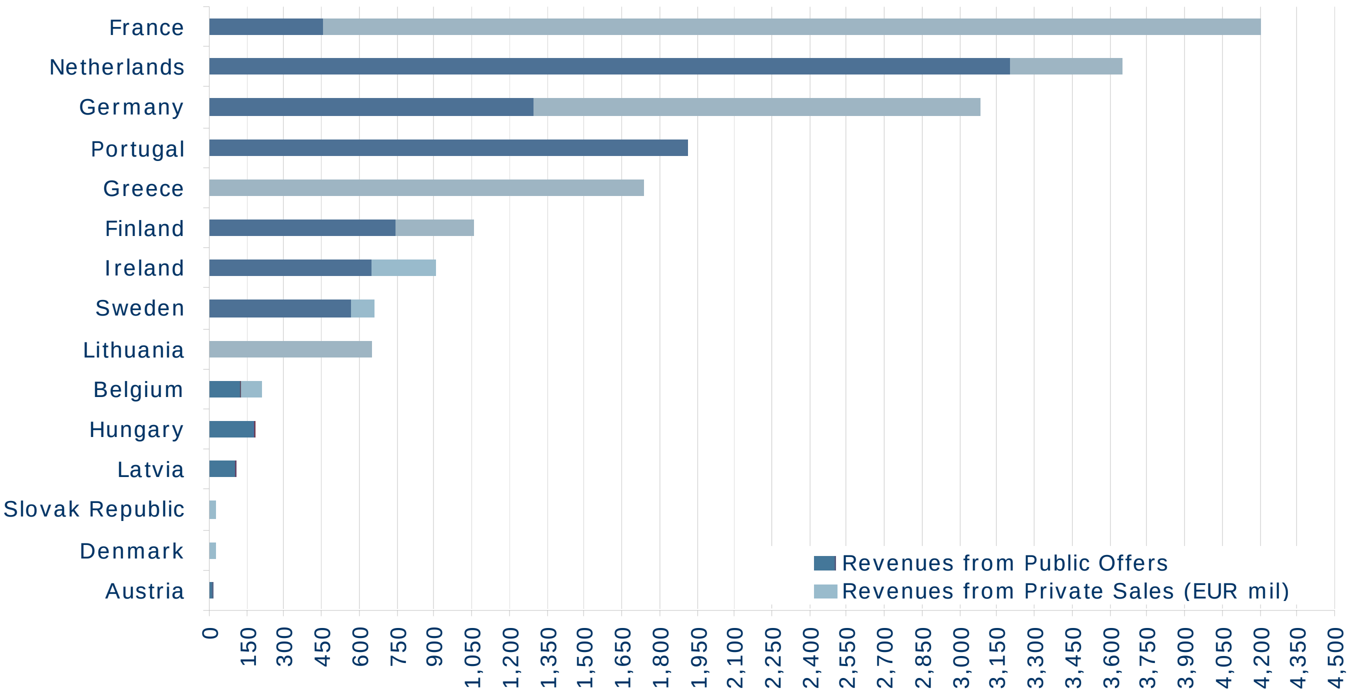
The unstoppable rise of private equity funds…

The investment banking business has radically changed in the last years and the rise of private equity represents an important element in this transformation. According to recent accounts, the 2,700 private equity funds have raised more than US$300 billion in 2006, and reached the stellar value of US$2 trillion in terms of aggregate purchasing power. Such an increase in scale is mirrored in the sheer size of the deals currently achieved and in the wide scope of activity. Privatization outcomes in 2006 have been strongly affected by this new trend. First, the €27 billion raised by private equity placements account for 66 percent of total revenues, one of the largest share ever achieved in Europe. Second, private equity investors emerged as the single most important set of buyers of privatized assets in 2006. Private equity funds have been winning bidders in 3 out of the top five privatizations, and in total purchased assets worth €5 billion.

…and their dramatic impact over corporate governance of privatized firms

The economic implications of the rise of this new type of investors are starting to appear. Their large stakes allow them to exert a significant influence in the corporate governance of privatized firms. Reportedly, Blackstone, one of the largest US funds, played a key role (together with the German government) in the recent resignation of Deutsche Telekom's CEO, giving a voice to investors disappointed by the continuing decline in stock prices. Such private equity groups will certainly remain the most attractive bidders for divesting governments. The Swedish government has warmly welcomed their involvement in the future privatization process, and some of most active funds (such as US based Cerberus led by former US Secretary of the Treasury John Snow, and 3i, one of the world's leaders in private equity and venture capital) have expressed interest in purchasing infrastructure assets which will be soon placed on the market by the German government.

Figure 4. Distribution of Privatization Revenues by Country, 2H2006



Source: *Privatization Barometer*

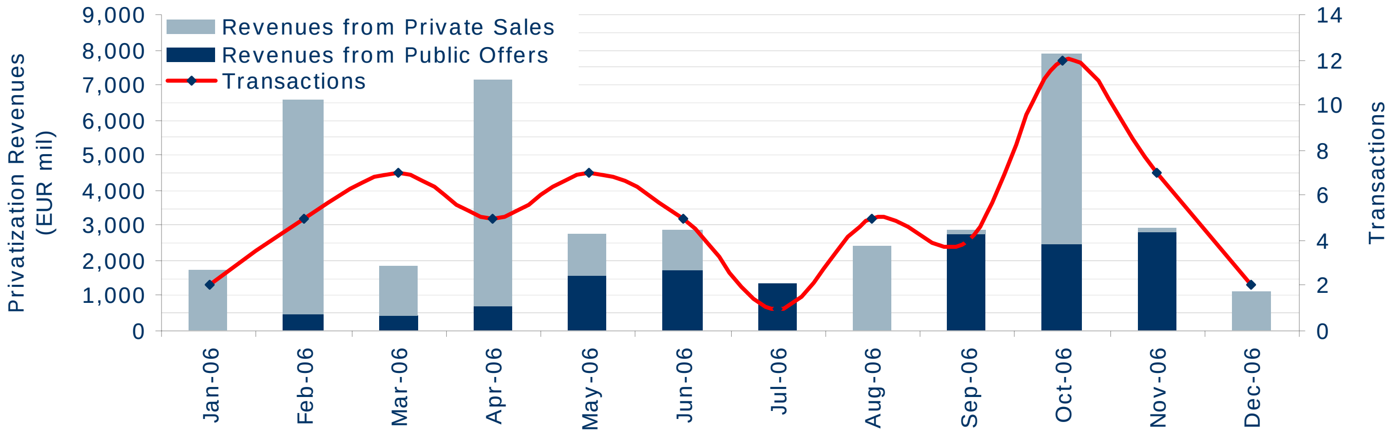
During 2H2006, share issue privatization – and particularly accelerated transactions – bounces back….

While private sales remained the preferred method, 2H2006 marked a definite resumption of share issue privatization, or offering shares on equity markets. After the plunge caused by the tightening of monetary policy, European stock market progressively gained ground and closed 2006 with a 18 percent increase reported over the year. Governments took advantage of this positive outlook on the stock market by launching five successful IPOs and especially seven accelerated seasoned underwritings. GalpEnergia, the Portuguese oil and gas operator, and Aéroports de Paris were certainly the most remarkable IPOs of the year, totaling €2.9 billion. The revenues raised by accelerated transactions (€4.5 billion) are even more impressive. This highly competitive placing method has progressively gained market shares in SEO, and surpassed 80 percent in government initiated secondary issues. Three of the four largest share issue privatizations, two involving the Dutch Koninklijke TPG NV-TNT and KPN and one Deutsche Post AG, are accelerated bookbuilt offerings earmarked to institutional investors. Financially pressed divesting governments have almost abandoned the classical fully marketed (and strongly underpriced) follow-on offering which typified large scale privatization in the 90s.

Old vs New Europe: the usual 10 percent solution

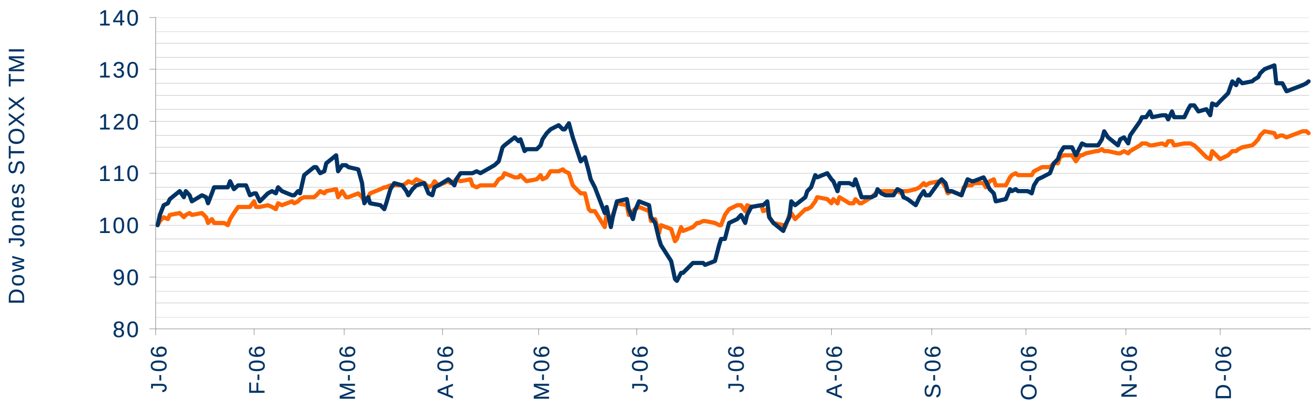
The 2006 country ranking confirms the "golden rule" on privatization activity: the New Europe gets around 10 percent of revenues with 13 deals, mainly executed during the 1H2006. Old Europe gets the lion share with almost a half of sale proceeds raised by two countries, France and Germany.

Figure 5. Total Privatization Revenues and Transactions in the Enlarged Europe, 2006



Source: *Privatization Barometer*

Figure 6. Equity Markets in EU25, 2006



Source: Elaborations on *Datastream*

An impressive 2006 in France

With presidential elections round the corner, the French privatization process will certainly slow down in 2007. Reportedly, the controversial merger between GdF and Suez (involving a further "privatization of GdF) will remain on hold until a new government is elected. Nevertheless, the results achieved by the French government in 2006 has been impressive on different dimensions. With activity quite evenly split between direct sales by the central governments and spin-offs of state-owned companies, the de Villepin administration has executed one the largest deal of the year, the €3.3 billion placement of Pages Jaunes to the US private equity fund KKR, has brought back profitably to the market Alstom, after a successful bailout, and finally conducted the successful floatation of Aéroports de Paris, the second largest IPO of 2006.

The two German drivers: KfW and regional governments

After a difficult 2005, Germany is back on track. The grand coalition led by Angela Merkel has solved the initial political uncertainty and found a sustainable path for fiscal consolidation. The €8.9 billion raised in 2006 have certainly contributed to relieve a financially distressed German budget. A key player in the revival of the process have been the KfW, the state-controlled financial holding company, which first sold a large stake in Deutsche Telekom to the US fund Blackstone and then reduced its holdings in Deutsche Post via an accelerated transaction on the market. Real estate privatization by local governments of Dresden and Hamburg has a great bearing on the revenues reported for the financial sector, together with the important and above cited deals involving large regional banks.

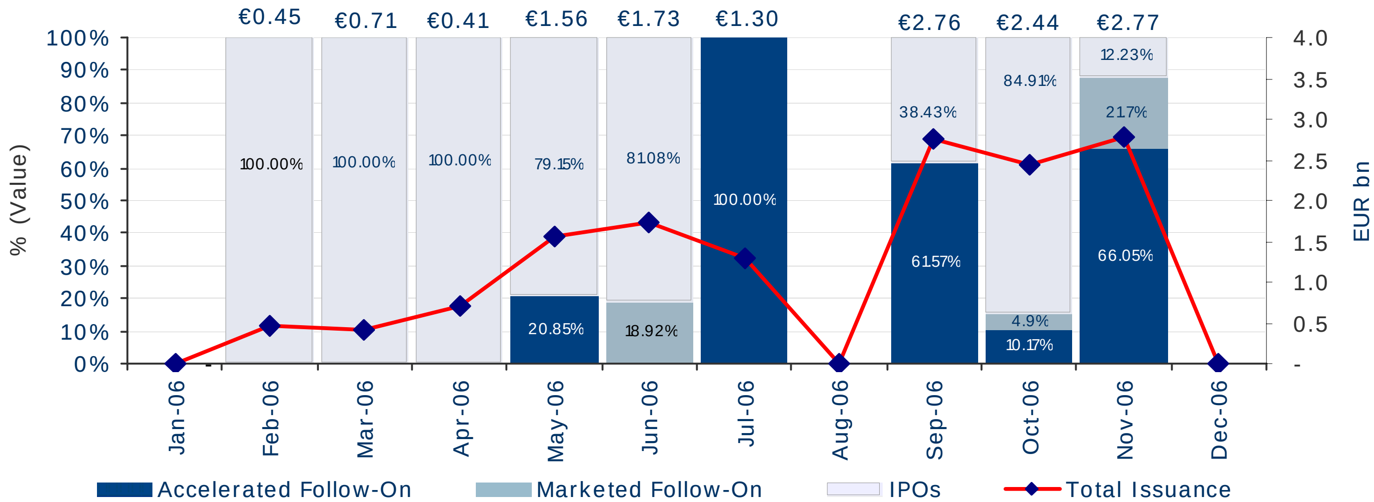
A noteworthy activity in the Netherlands and (again!) in the UK

Among other top privatizing countries, a small country such as the Netherlands sticks out with more than €5 billion raised in 4 sizable deals. The privatization laggard UK almost reached the same amount mainly thanks to its gigantic private equity placement of Westinghouse recorded last February, then disappeared again in 2H2006.

Quo vadis, New Europe?

Privatization in New Europe is in the doldrums and politics is the culprit. One of the most revealing examples of successful transition to market economy, Poland, has apparently abandoned the road to economic reform and privatization under the guidance of powerful populist leaders such at the twins Kaczynski. The Czech Republic and Slovakia have also slowed down the divestiture process after elections altering the political climate. The only countries which have proved a strong commitment to privatization and market reform are Hungary and Lithuania, where privatization advanced in the petroleum industry.

Figure 7. Share Issue Privatization in the Enlarged Europe, 2006



Source: *Privatization Barometer*

Privatization activity almost evenly split between the two semester, with differences in the methods…

As Figure 5 shows, privatization activity in 2006 is quite evenly split between the two semesters. The amount raised in 2H2006 is €18.4 billion and it accounts for 45 percent of the yearly total. A remarkable difference appears in the privatization methods chosen by divesting governments, with share issue privatization gaining ground over private sales in 2H2006. The positive outlook on equity markets is largely responsible for this shift, and governments rapidly took advantage of this opportunity by swiftly implementing some secondary issues.

..and swaps between countries and sectors…

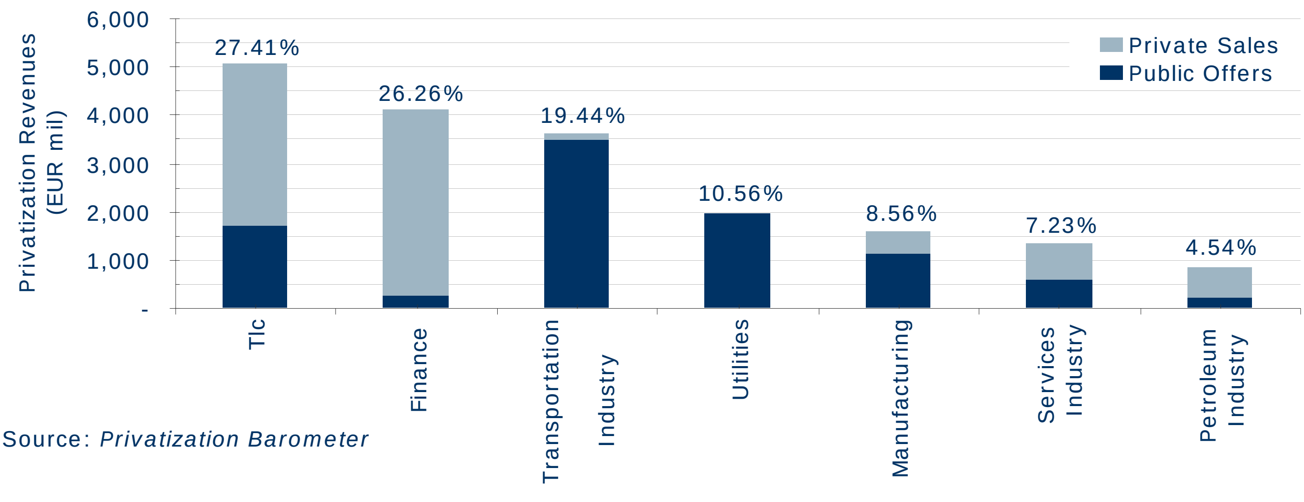
The telecommunication sector attracted the most important deals of the 2H2006, immediately followed by the financial industry, which keeps the prominence reported in 1H2006. The manufacturing sector loses ground in favor of the transportation industry mainly thanks to the important sales in the postal sector. Some changes also appear in the country ranking. With respect to the first half of the year France and Germany swap from the first to the third positions, while the Netherlands surpasses the United Kingdom to close in third place in the full 2006 ranking (see Figure 2 and 4). In New Europe, privatization almost vanished in the course of the year, with only four countries involved and less than €1 billion raised. As we already noted, for the first time since the early 90s, Italy does not appear in this ranking.

Looking ahead, privatization will reach a plateau in 2007…

…but Sweden will make a fresh start

To conclude, we advance our regular forecast on privatization for 2007. After the increasing trend started in 2002 and the correction reported last year, privatization has likely reached a plateau. Thus total European transaction values in 2007 are not expected to fall below €40 billion. Germany will certainly remain next year's privatization heavyweight. The German government will push forward divestiture involving the KfW and with important sales in infrastructure and in the financial industry. Sweden will finally launch large scale divestiture. The young new leader Mr. Reinfeld has promised a shake up in the Swedish social model with a pro-market program largely based on state assets divestiture, which should start yielding significant revenues soon. Political uncertainty surrounding elections will slow down activity in France, one of the engines of recent privatization trends. Nevertheless, some important deals in the financial sector currently underway will see the light. As regards to the countries of the New Europe, we do not expect a definite resumption of the process during 2007. Nevertheless, Hungary should be the most active country, while the Czech Republic and Poland should accomplish ongoing sales in the utilities.

Figure 8. Distribution of Privatization Revenues by Sector, 2H2006



Source: *Privatization Barometer*

William L. Megginson

University of Oklahoma

Major Deals of 1H2006

Second half of 2006: a surge in global privatization activity

The second half of 2006 witnessed a surge in global privatizations, with a total value of €56.65 billion ($73.65 billion), which brought the full-year 2006 total to a very respectable €90.55 billion ($115.95 billion). This makes the 2006 privatization total the sixth highest annual dollar value overall, and marks the first time since 2000 that global divestment proceeds totaled over $100 billion for two years in a row. In that sense, 2H2006 marks the continuation of a trend of steadily increasing annual privatization sales that began after proceeds hit a decade low in early 2003.

…representing a sharp break from traditional privatization patterns

In a more profound sense, however, last semester's total represents a sharp break from traditional privatization patterns, in that the €18.4 billion ($23.4 billion) raised by EU governments through 16 share issue privatizations and 15 asset sales represented less that one-third of the global privatization total. Four offers from the former Soviet-bloc countries of Russia, Serbia, Bosnia-Herzegovina, and Kazakhstan raised €11.67 billion ($15.17 billion) or two-thirds as much as the EU combined, while a single Australian offering raised €9.16 billion ($11.90 billion). However, China was by far the most important privatizing country of 2H2006, raising more in two share offers--€18.23 billion ($23.70 billion)--than the EU did in 31 total sales. Most notably, the October IPO of a 10 percent stake of Industrial and Commercial Bank of China (ICBC) raised an astonishing €16.31 billion ($21.20 billion), making this the largest initial public offering in world history. Coupled with the €9.93 billion ($12.91 billion) raised in two offerings during 1H2006, China raised €28.16 billion ($36.61 billion) through four massive share issue privatizations during 2006, and led the world in the total value of IPOs for the year.

China's lion's share

Sales in Old Europe during 2H2006

Trends in privatizations across Old Europe countries

There were thirteen large privatization sales, raising at least $500 million, in Old Europe during 2H2006, and these collectively followed several patterns established recently. First, private sales accounted for six of these deals, including the two largest, and four of the sales (including the largest) were indirect privatizations by state-owned enterprises rather than by the central government itself. Second, three of the four largest share issue privatizations were executed through accelerated underwritings. Third, private equity investors were the buyers in three of the large deals, including the largest, France Telecom's October private sale of its 54 percent stake in Pages Jaunes to Kohlberg Kravis and Roberts (KKR), which raised €3.31 billion ($4.30 billion). KKR actually beat out another US private equity fund to win this prize, which capped a frenetic multi-year period of KKR investment activity in EU privatizations.

The European banking sector consolidation continues apace

The second largest EU privatization during 2H2006 represented another trend of sorts—the ongoing (and painful) consolidation of the European banking sector. In August, the French bank Crédit Agricole acquired a 52.55 percent stake in Greece's state-controlled Emporiki Bank for €1.74 billion ($2.26 billion). Though successful, the sale raised less than the Greek government had hoped, in large part because a mooted competing bidder did not ultimately materialize. Emporiki's publicly traded shares dropped by 2.3 percent when it was announced that Crédit Agricole had achieved a majority stake.

Two other noteworthy bank sales during 2H2006 occurred in Germany. In October, the large German bank West LB sold its 24.1 percent equity stake (26.6 percent voting stake) in the public-sector regional bank HSH Nordbank to a private equity group led by American investor Christopher Flowers. This sale raised €1.27 billion ($1.65 billion), after the regional bank's other (public sector) shareholders passed on their right of first refusal to buy additional shares. That same month, the German government sold a 10 percent stake in Landesbank Berlin Holding AG (Bankgesellschaft Berlin) to DSGV, the association of German savings banks, for €407 million ($529 million). This sale had to withstand a court challenge, because DSGV is a quasi-state association and was bidding for Landesbank Berlin primarily to keep it out of the hands of an aggressive private buyer. The sale was ultimately approved, however, on the grounds that DSGV paid a market price for the target bank.

Accelerated book-built offerings are today the largest privatizations in public equity markets

As noted earlier, three of the four largest share issue privatizations of 2H2006 were executed through accelerated underwritings—specifically through accelerated book-built offers (ABOs). The Dutch government executed two of these, the €1.50 billion ($1.95 billion) offering of a 10.9 percent stake in Koninklijke TPG NV-TNT in November and the September ABO of its residual 8 percent stake in Koninklijke KPN NV, which raised €1.7 billion ($2.2 billion).

Table 1. Deals, 2H2006

Date	Company Name	Nation	Sector	% for Sale	Value (€ mil)	* Direct/ Indirect	Method of Sale
10/11/06	Pages Jaunes (France Telecom)	France	Telecommunications	54.00	3,312.00	Indirect	Private Sale
08/08/06	Emporiki Bank	Greece	Finance & Real Estate Industry	36.56	1,740.00	Direct	Private Sale
09/30/06	Koninklijke KPN NV	Netherlands	Telecommunications	8.00	1,700.00	Direct	Accelerated Transaction (AT)
10/24/06	GalpEnergia	Portugal	Utilities	23.00	1,500.00	Direct	Initial Public Offering (IPO)
11/21/06	Koninklijke TPG NV - TNT	Netherlands	Transportation Industry	10.90	1,499.92	Direct	Accelerated Transaction (AT)
07/12/06	Deutsche Post AG	Germany	Transportation Industry	6.10	1,298.70	Direct	Accelerated Transaction (AT)
10/20/06	HSH Nordbank AG	Germany	Finance & Real Estate Industry	24.10	1,271.89	Indirect	Private Sale
12/16/06	Mazeikiu Nafta	Lithuania	Petroleum Industry	30.66	650.08	Direct	Private Sale
09/27/06	Aer Lingus	Ireland	Transportation Industry	60.00	644.99	Direct	Initial Public Offering (IPO)
10/28/06	Rezidor Hotel Group AB (SAS)	Sweden	Services Industry	58.30	571.97	Indirect	Initial Public Offering (IPO)
12/12/06	SDU	Netherlands	Manufacturing	100.00	450.00	Direct	Private Sale
09/10/06	Outokumpu Technology (Outokumpu Oyj)	Finland	Manufacturing	80.00	416.27	Indirect	Initial Public Offering (IPO)
11/14/06	Portucel - Empresa Nacional de Celulosa	Portugal	Manufacturing	25.70	415.32	Direct	Public Offering
10/04/06	Landesbank Berlin Holding AG	Germany	Finance & Real Estate Industry	10.00	407.40	Direct	Private Sale
11/29/06	EDF Energies Nouvelles (EdF)	France	Utilities	20.22	339.29	Indirect	Initial Public Offering (IPO)
08/31/06	Kapiteeli Oyj-Hotel Portfolio, 15 units	Finland	Services Industry	100.00	304.50	Direct	Private Sale
10/23/06	ICADE SA-Real Estate Property Portfolio	France	Finance & Real Estate Industry	100.00	299.88	Direct	Private Sale
11/15/06	Outokumpu Oyj	Finland	Manufacturing	6.63	296.75	Direct	Accelerated Transaction (AT)
08/24/06	Great Southern Hotels Ltd- Hotels, 7 units	Ireland	Services Industry	100.00	263.76	Direct	Private Sale
11/21/06	MOL	Hungary	Petroleum Industry	1.73	186.94	Direct	Public Offering
11/24/06	EDF Capital-Investissement SA	France	Finance & Real Estate Industry	100.00	134.23	Indirect	Private Sale
10/12/06	GIMV	Belgium	Finance & Real Estate Industry	12.94	131.51	Direct	Accelerated Transaction (AT)
10/17/06	ICADE SA	France	Finance & Real Estate Industry	4.18	116.74	Direct	Accelerated Transaction (AT)
10/05/06	Ventspils Nafta	Latvia	Utilities	38.60	106.52	Direct	Public Offering
09/27/06	VVR-Berek GmbH	Germany	Services Industry	100.00	103.71	Indirect	Private Sale
10/28/06	Rezidor Hotel Group AB (SAS)	Sweden	Services Industry	10.00	87.99	Indirect	Private Sale
08/03/06	ABX LOGISTICS Worldwide SA/NV (SNC)	Belgium	Transportation Industry	100.00	78.53	Indirect	Private Sale
11/30/06	Finnlines Oyj (Stora Enso Oyj)	Finland	Transportation Industry	5.43	35.45	Indirect	Accelerated Transaction (AT)
02/10/06	Kosice International Airport	Slovak Republic	Transportation Industry	66.00	25.33	Direct	Private Sale
08/23/06	Fifth FM	Denmark	Telecommunications	100.00	24.63	Direct	Private Sale
10/10/06	Telekom Austria AG	Austria	Telecommunications	0.20	13.57	Direct	Public Offering
Total	**31 Transactions**				**€18,427.85**		

* Direct Privatizations refer to the sale of government's direct stakes. Indirect Privatizations include spin-offs and transfer of shares from government owned companies. Parenteses report the Parent/Seller Company name.

Source: *Privatization Barometer*

The third significant ABO was the German government's July sale of a 6.10 percent stake in Deutsche Post AG, which raised €1.30 billion ($1.69 billion). Government reliance on accelerated underwritings for disposal of stakes in state enterprises mirrors practices in Europe's private sector, where the three types of accelerated seasoned equity underwritings (especially ABOs) now account for over two-thirds of the value of SEOs.

Successful Privatization IPOs Demonstrate Continued Retail Investor Interest

Portuguese IPOs

Despite being dominated by private sales and accelerated underwritings, Old Europe's privatization landscape during 2H2006 was not devoid of old fashioned IPOs and marketed seasoned equity offerings (SEOs). There were four large IPOs and one SEO during this semester. The October IPO of a 23 percent stake in GalpEnergia by the Portuguese government was the forth largest sale overall in the EU during this period, and raised €1.50 billion ($1.95 billion). This offering, Portugal's third largest privatization ever, was over-subscribed and the shares closed up 3.8 percent in their first full day of trading. Portugal also executed the only major SEO in Old Europe during 2H2006, the November sale of 25.7 percent of Portucel-Empresa Nacional de Cellulosa, which raised €415 million ($540 million).

The controversial sale of Air Lingus

The second largest IPO of 2H2006 was also one of the most contentious share offerings in recent European history, less for what happened in the offering itself than what occurred after the offer closed. After more than six years of unsuccessful efforts, the Irish government was finally able to sell a 60 percent stake in Aer Lingus in September, raising €645 million ($839 million) in the process. Even so, the offer was priced at the low end of its indicated price range, and was only possible after the government and managers had overcome significant opposition from the airline's unions--which own 9.9 percent of the company through their share ownership trust. Almost immediately after the IPO closed, the unthinkable happened—Ryanair launched a hostile takeover bid for its long-time and frequently derided Irish rival! This surreal bid played out against a background of unrelenting hostility from Aer Lingus, the Irish government, and the airline's unions, and was soon challenged by the European Commission on antitrust grounds. In January 2007, Ryanair admitted defeat and withdrew its bid, though the discount carrier reiterated its desire to ultimately acquire Aer Lingus.

The temperature is rising Nordic countries

The last two large Old Europe IPOs came from Scandinavia. In October, Sweden's SAS raised €572 million ($744 million) with an IPO of a 58.3 percent stake in Rezidor Hotel Group AB. Though the offer was nine times subscribed, the shares closed 2.4 percent below the offering price on the first day's trading. Even as SAS reduced its stake in Rezidor, however, the firm's other major shareholder—the U.S. travel company Carlson—increased its stake from 25 to 35 percent. Finally, the Finnish state-controlled firm Outokumpu raised €572 million ($744 million) through a September IPO of an 80 percent stake in Outokumpu Technology. A later exercise of the over-allotment option resulted in an additional 8 percent being sold. The IPO was also nine times over-subscribed but, unlike Rezidor, the shares closed up 3.31 percent on the first trading day.

Sales in New Europe during 2H2006

A light 2H2006 in New Europe

The second half of 2006 was a very light privatization period for New Europe's governments. There were only four sales, which collectively raised less than one billion euros. The only sizable deal was the culmination of the tortured sale of Lithuania's only oil refinery, Mazeiku Nafta, to Poland's PKN Orlen. This deal was negotiated in 1H2006 (and was described in the last Newsletter), but only closed in December. The Lithuanian government sold PKN Orlen a controlling 30.66 percent stake in Mazeiku Nafta for €650 million ($845 million).

Sales outside of Europe during 2H2006

Outside Europe, Russia launched Rosneft' share issue after Yukos affaire…

As noted in the introduction, 2H2006 was unique in that two-thirds of all privatization proceeds were raised by sales outside of the European Union. Seven large sales in Eastern Europe, Asia and Australia raised no less than €39.05 billion ($50.77 billion), and three of these were truly gargantuan share issue privatizations of historically problematic companies. In July, the Russian oil company Rosneft raised €8.00 billion ($10.40 billion) in an IPO of primary shares that was very well received by retail investors (and closed the first day at the offering price), but failed to attract large numbers of institutional investors. This may have been partly due to the controversy surrounding the Russian government's effective expropriation of the assets of Yukos, and questions about the Kremlin's general respect for foreign investors' property rights. Nonetheless, 60 percent of this offering was raised in London in the form of global depositary receipts, with the remainder being sold in Moscow.

A large seasoned issue by Australian Telstra…

The second large SIP of 2H2006 was Australia's divestment of a third tranche in Telstra, which raised €9.15 billion ($10.40 billion). After a smashing IPO in 1997 and an equally successful SEO in 1999, Telstra's stock performed as abysmally as other telecom shares after the tech bubble burst in 2000. In addition, Telstra's managers had been waging a long battle with the Australian government over tariff rates and other regulatory issues for several years. For all these reasons, the government initially planned to sell only a 17 percent stake in the third offering, but strong demand led to a doubling of the stake sold to 34 percent and the November offering was substantially oversubscribed.

China boasts the largest IPO in history: ICBC

Impressive as these offers were, they were dwarfed by the largest IPO in world history, the €16.31 billion ($21.20 billion) primary share offering of Industrial and Commercial Bank of China (ICBC), executed in Hong Kong and Shanghai in October. This offering was massively over-subscribed, with total orders exceeding $500 billion being placed for the 15 percent share of the company on offer. The first day return to Hong Kong investors was 15 percent, while Shanghai investors earned a 5 percent initial return. Amazingly, the Chinese government had been forced to recapitalize ICBC and other state-owned banks less than two years previously.

Rounding out the non-EU privatization sales of 2H2006 are two IPOs and two telecom asset sales. In July, the Chinese government executed the domestic IPO of Bank of China, raising €1.92 billion ($2.50 billion) in a primary share offering that was 50 times oversubscribed and which yielded a 23 percent first day return to its initial investors. Three months later, KazMunaiGas, the Kazakh oil exploration and production company, executed a primary offering of 8.7 million shares, structured as GDRs, in London and 17.9 million shares on the Kazakhstan

Stock Exchange. The IPO raised €1.56 billion ($2.03 billion), was heavily oversubscribed, but closed at the offer price at the end of the first day's trading.

TLC strike back in central Europe

Two telecom asset sales in Central Europe complete the list of significant privatizations during 2H2006. In July, the Serbian government sold its 100 percent stake in the mobile phone service provider Mobi 63 in an auction, which Norway's Telenor won with a bid of €1.51 billion ($1.90 billion). This was the largest ever Serbian privatization, and the government only had the shares to sell because the previous majority owner had defaulted and fled the country. Finally, in October, Bosnia-Herzegovina sold its 65 percent stake in the telecom service provider Telekom Sprske in an auction that raised €646 million ($840 million). While successful and also the largest in Bosnia-Herzegovina's history, this sale was controversial because the winning bidder was Serbia's state-owned operator Telekom Srbjia—which offered half-again as much as the next highest bidder, Telekom Austria.

Andrea Levantini

Executive Director, Morgan Stanley - Global Capital Markets

The Role of Private Equity Funds in Global Privatizations

The growth of Private Equity Funds worldwide

The rise of private equity funds has been dramatic in last years …

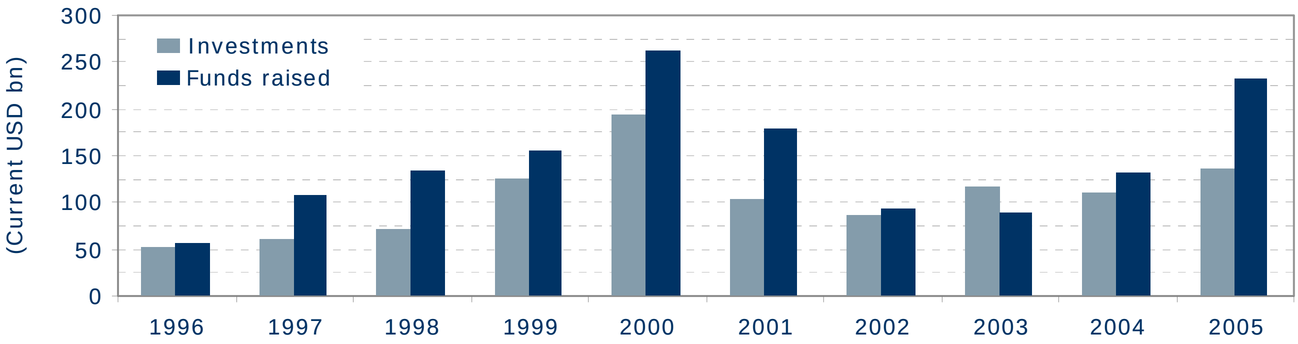
Private Equity Funds ("PEFs") are large pools of capital managed by professional investors that are active in non publicly traded securities. Many of the largest Private Equity Firms have more than one fund under management, most often organized by scope or industrial sector of activity. The life of a single fund extends up to ten years during which the fund managers will typically make between 15 and 25 separate investments, with usually no single investment exceeding 10 percent of the total fund commitments. Participation in these funds is limited to institutional investors or high net worth individuals who can afford to have their capitals locked-in for a long period of time, as such participations are not freely tradable like mutual fund interests.

…and they are commonly recognized as key players in the global M&A activity

The PEFs' ability to execute innovative capital structure solutions and their successful track record of high returns on investments, often in excess of 30 percent per year, have been the driving forces behind their impressive growth over the last fifteen years. It is estimated that there are now 2,700 PEFs active around the world with a collective capital spending power of up to $ 500 billion. More than 100 of these funds are bigger than $1.0 billion and some have more than $10 billion of money under management. Given the average debt to equity ratio (1:4) the PEFs normally apply to their investments, this available capital translates into an impressive $2.0 trillion of purchasing power. Unsurprisingly, in 2006 the PEFs originated deals accounted for 25% of global merger and acquisition activity and 30% of debt high yield and IPO transactions.

In spite of the above, the PEFs to date have been marginal players in global privatizations, with only few direct investments completed. In this brief article, we discuss the reasons behind this low level of activity in the past, but also explore the PEFs' potentially pivotal role in the growing trend of private equity placements by divesting Governments.

Figure 1. Global Private Equity, 1996-2005.



Source : IFSL Estimates Based on EVCA/Thomson Financial/PwC, Aper Data.

A brief overview of the PEFs strategies

However so far PEFs have only had a marginal role in privatization deals. Why?

Generally speaking, we can divide the PEFs in three broad groups: *a)* those that invest in start up firms (venture capital funds), *b)* those that invest in rapidly expanding firms and/or sectors (growth funds), and *c)* those that invest in the buy out and restructuring of mature companies (leverage buy-out funds).

Investments *sub a)* and *sub b)* are by their natures of very difficult application to Government owned companies, therefore the managers of such funds have rarely looked into privatizations. Yet, those same funds have been quite active in the subsequent spin-offs of some of the privatized assets or in the following sale or restructuring by the initial acquirers.

Investments *sub c)* have counted for the vast majority of the capital invested by the PEFs over the last two decades worldwide. Acquisition candidates were companies with significant restructuring potential and/or with visible future cash flows. Yet, although many of the companies privatized worldwide in the period shared these characteristics, privatizations have not formed a meaningful part of the portfolios of the PEFs. On the surface, there is no obvious reason why this has not happened.

The reasons behind historical low intervention in privatizations by the PEFs

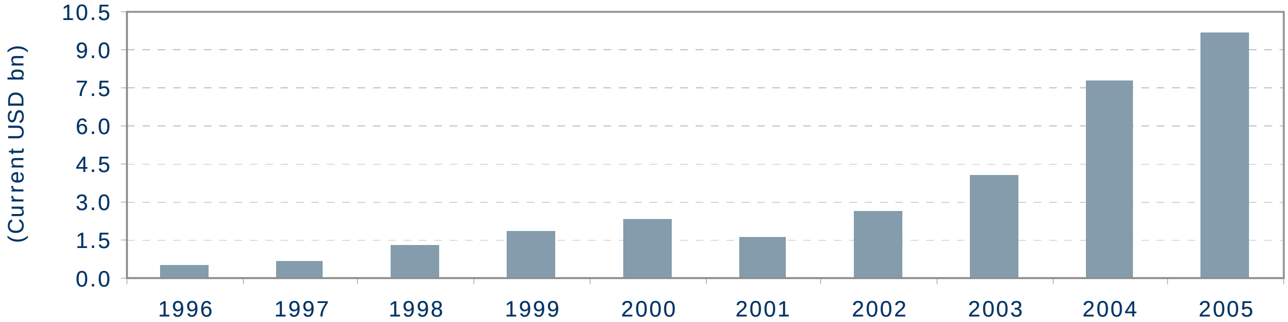
Governments' skepticism towards this type of investor is the basic explanation

The PEFs have definitely not deliberately neglected per se the huge privatization opportunity, nor were the sizes or the costs of the investments impediments to them. The PEFs, which nowadays often pool their forces in club deals, have in fact acquired and can consider acquisitions of assets for up to $50 billion in value. Moreover, in today's low cost of debt environment, the PEFs are often able to pay higher valuations than those affordable by strategic buyers.

The reality is that the PEFs have not participated actively in privatizations because of a combination of factors, ranging from a generic governmental skepticism towards PEFs to the privatization procedures used, from the sector of activity of the divested companies to the regulatory constraints imposed in many privatizations.

For years, the Governments worldwide have been very suspicious of PEFs' intervention in privatizations because it was perceived as overly lucrative and possibly value destroying for the acquired companies. Governments were also not accustomed to the PEFs' high recourse to leverage and were afraid of criticism arising from the unions and the public based on expectation of severe cost cuttings.

Figure 2. Global Private Equity Secondary Market.



Source : The Private Equity Analyst (1996-2003 Data); Triago (2004 and 2005 Data).

Private equity funds need control and this has typically not been relinquished by divesting governments

The processes used by Governments to privatize their assets have also proven to be unfriendly to the PEFs. With very few exceptions, the buy-out firms require to obtain board control of the acquired companies in order to appoint the key executives and have the necessary flexibility to execute the desired operating and financial restructuring. To this respect, a retrospective analysis of the privatization processes used globally shows that direct negotiations to sell State owned companies have, also for political reasons and irrespective of the price offered, most often resulted in sale to industrial or strategic partners at the disadvantage of pure financial investors. Conversely, where the recourse to broad public ownership distribution was chosen, like in the many privatization IPOs, the PEFs were not permitted to obtain the required majority control by virtue of the allocation mechanism of the IPO process itself.

Regulatory constraints also limited their involvement as buyers

With regards to the limits on the PEFs deriving from the sectors of activity of the privatized companies and the regulatory constraints imposed, it should be noted that many of the large global privatizations have been completed in tariff regulated sectors (communications, transportations) or in sectors with stringent employment level constraints (utilities, former municipalities) or, finally, in the banking or insurance industries, where the recourse to aggressive leverage is not permitted. All of the above reasons made it highly impractical for the PEFs to play a centre stage role in past privatizations.

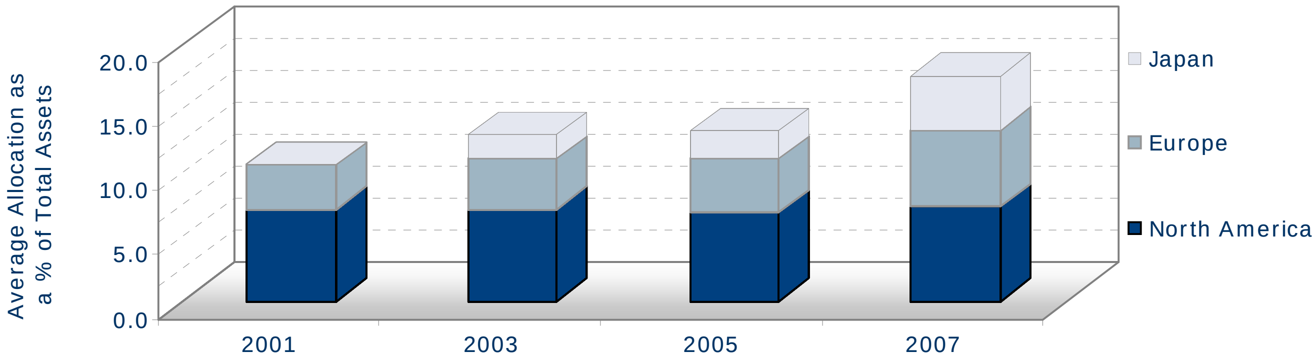
Will the PEFs be important players in future privatizations?

What should we expect in the future? Are the obstacles still there preventing the PEFs from playing a significant role in privatizations? Probably not, and for many reasons.

Today governments, when privatizing, are not as unfriendly to PEF investing methods as they used to be in the past…

On the practical side, Governments and labor representatives today accept more easily the PEFs' investing methods. They impose far less minimum employment levels and tariff constraints as long as the PEFs can show that the financial and operating engineering used by them does not harm the companies' ability to invest and expand their businesses. Concurrently, many of the largest PEFs have developed Special Situations strategies broadly defined as non-traditional use of their capital in order to exploit various types of anomalies or opportunities in a company or an industry. Anomalies like the pricing arbitrage between different securities of the same company or any loophole in the corporate governance of a firm, or opportunities like unlocking hidden value by disaggregating the operating business by the holding companies, or consolidating fragmented value chains or providing short term mezzanine lending, and many others.

Figure 3. Institutional Investment in Private Equity by Area, 2001-2007



Source : Russell Investment Group, Adveq.

These strategies in many cases have been and will be addressed to large deals especially in the public utilities or infrastructures sectors or to the acquisition of participations in public companies still controlled by Governments.

Private equity and corporate governance: a successful story, apparently

More fundamentally, the PEFs' experience may change the future of privatizations because PEFs are in essence a new model of management applicable to any company. In fact, the PEFs' ability in purchasing undervalued assets and making use of financial engineering to yield superior returns is only part of the PEFs' successful story. The other and more important part of the story is the PEFs' ability to add value exploiting the large information gap between what the management knows and what the public shareholders (or the Governments for our purposes) know. By heavily restructuring or re-motivating the board of directors of the acquired companies, the PEFs effectively replace distant, unfocused public ownership supervision with the monitoring of better-informed and more highly motivated owners. This is achieved also via the alignment of company management's interest with that of the ownership through the introduction of powerful equity incentives. In essence, the job of PEFs is that of improving the performances of the companies they invest in by way of providing a set of skills and tools which either are not present in the company or are not used. This apparently simple value creating strategy could be replicated in many large companies, thereby including many of those still under Government control.

Blackstone's lesson in pushing for change in Deutsche Telekom

We should therefore expect an increasing level of attention by the PEFs for the upcoming privatizations or follow-ons. The Blackstone's €2.7 billion leveraged investment in Deutsche Telekom was one of the most interesting private equity deals of the year. With no intention of ascertaining the merits of such investment,

Table 1. Top 10 Countries for Private Equity Investments, 2004-2005.

Country	Investment Value (USD bn) 2004	Investment Value (USD bn) 2005	% Share 2005	As % of GDP 2005
US	43.8	53.3	40	0.4
UK	22.4	29.6	22	1.3
France	6.1	9.1	7	0.4
Sweden	1.9	3.7	3	1
Spain	2.3	3.4	3	0.3
Germany	4.4	3.4	3	0.1
Netherlands	1.9	2.9	2	0.5
Japan	7.1	2.1	2	0
others	10.1	30.3	20	0.2
Total	110	134.8	100	0.3

Source : IFSL Estimates Based on EVCA/Thomson Financial/PwC, Aper Data.

Table 2. Largest Private Equity Transactions.

Announcement Date	USD bn	Number of Sponsors
HCA (06/06)	33.0	3
RJR Nabisco (10/88)	30.2	1
BAA (03/06)	30.2	1
Kinder Morgan (05/06)	26.5	4
Albertsons (01/06)	17.4	1
Hertz (09/05)	15.1	3
Univision (06/06)	13.4	5
VNU (03/06)	11.6	6
SunGard Data Systems (03/05)	10.8	7
TDC (11/05)	10.6	5

Source : Dealogic, Thomson Financial, Economist.

what is important is that the "certification role" played by that investment was widely regarded as a positive for DT and is a clear sign of the above-mentioned new focus by PEFs. Will this immediately evolve in more PEFs (or other skilled private investors) intervention in large companies still under Government control? It is hard to tell, but there is no reason why large public companies should not consider inviting some of these skilled investors onto their boards ahead or during a privatization process, as a "certification guarantee" for the broader investor community. By doing so, they would de facto replicate what is happening in the corporate world, where we currently note a much higher level of shareholders' activism brought in by the most important hedge funds. Such an innovating process would allow the State owned companies to achieve the necessary monitoring and transparency ahead of more complicated privatizations, ultimately realizing higher selling values.

On the PEFs side, it appears that they are eagerly preparing for such possible evolution, through the recent development of highly focused niche strategies, hiring managers with deep turn-around knowledge and sector expertise. Finally, the PEFs understand well that they will surely fare better if they manage to engage in joint-venture style relationships with Governments before they fully commit their capital and resources to privatizations. We are these days witnessing the birth of these Joint Ventures for instance in the sector of infrastructure funds, where the access to large infrastructures by the Governments is paired with the access to capital and to professional management by the PEFs. We believe there are many other opportunities in the healthcare, technology, transportation and security sectors, just to name a few, in which the two different skill sets may be combined to create value to the investors and better services to the public.

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Spring of Hope or Land of Mines: Bank Privatization in China

Chinese banks were recently listed on stock markets with flying colors: the initial offered shares were oversubscribed and the after market performances of these shares have been quite strong (see chart 1). Have these Chinese banks succeeded in transforming themselves?

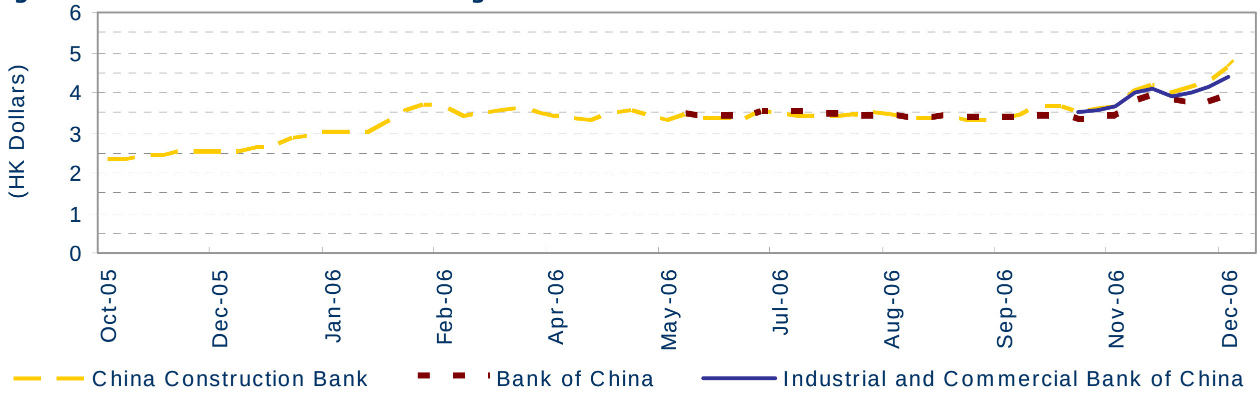
The recent floatations of big Chinese banks are some of the largest IPO in history

Initial public offerings (IPO) of Chinese banks are phenomenal; China Construction Bank (CCB) raised $9.2 billion in October 2005, Bank of China (BoC) $11.2 billion last May, and Industrial and Commercial Bank of China (ICBC) $21.9 billion in October. Except for Agriculture Bank of China, which is being significantly restructured, three of the four biggest Chinese banks are now listed in Hong Kong Stock Exchange. Both international investors and domestic investors overwhelmingly applied for IPO subscriptions and the post IPO performance of these banks has brought handsome returns to investors so far. During the period between the listing date and Christmas 2006, CCB's share price rose by 116%, BoC by 12% and ICBC by 25%.

Chinese Banks are quintessential for growth, but they are burdened by NPLs

The Chinese financial system is highly bank centered. Table 1 reports the percentages of different financing tools over total financing in China and bank loans are undoubtedly the majority. Among these bank loans, more than a half slice is taken by the big four. The performance of these banks is thus essential to the sustainable economic growth of China. However, they were once laden with bad loans and technically insolvent. According to Dai Xianglong, the former central bank governor, the ratio of combined non-performing loans (NPL) to the total loan portfolio was 35 percent in 1999 and 25 percent in 2000. The figure provided by China Banking Regulation Commission shows that it was as high as 26.2 percent in 2002. Some economists, like Nicholas Lardy, caution that the problematic banking sector may lead to a financial meltdown in China some day. There has not been a bank run so far, because depositors trust the Chinese government owner, although the government might itself run out of money one day.

Figure 1. Share Performance of the Big Three.



Source: HKEx.

Before IPOs, banks have been deeply restructured…

Before going public, the Chinese government made huge efforts to restructure these three banks. To clean up the banks' balance sheets, the government set up four asset management companies and the banks then wrote off hundreds of billions of dollars worth of bad loans. Besides this, the Chinese government directly recapitalized these banks with its foreign reserves and government bonds. For instance, the Bank of China and China Construction Bank received US$ 45 billion at the end of 2003. We illustrate the restructuring efforts and estimate the costs on recapitalizing these banks in table 2.

…and IPO proceeds go to the banks, not to the government

Furthermore, the sizeable IPO proceeds are not collected by the government owner, but retained in the banks themselves. By this, the Chinese government officially terms the public offerings of state-owned banks as ownership diversification instead of partial privatization. By the third quarter of 2006, the non-performing loan to total asset ratio was reduced to 9.31 percent. These Chinese banks have been a black hole of the Chinese economy and restructuring for oversea listings has been very costly to the Chinese government. Nonetheless, it remains to be seen whether large amounts of new bad loans emerge in coming years.

What is a good deal?

To better project the prospect of these banks, we need to understand why such a huge loss has been incurred during a period of extremely rapid economic growth in China. In brief, these bad assets resulted partly from the bankers themselves and partly from the government owner.

Corporate governance scandals in banks have been frequent

Internal controls of these banks were inadequate and there were many scandals involving Chinese bankers. Just three months before the oversea listing of China Construction Bank, the then president of CCB, Mr. Zhang Enzhao, was accused of corruption with taking bribes. As for Bank of China, the former Chief Executive Officer, Mr. Wang Xuebing, has been found guilty of misappropriating bank funds and breaking financial rules. One of his misdeeds resulted in fines of $20 million being levied on BoC by American and Chinese security authorities. Corruption is not limited to top dogs, but is a widespread plague in these banks. In Kaiping subbranch, a small town branch in the Guangdong province, two low-ranked bank managers diverted millions from Bank of China during a nine-year period and triggered a loss totaling $480 million for BoC in 2001. A former subbranch head in Heilongjiang province ran away with $120 million of clients' deposits in March 2005. In 2006, the manager of another small county branch pocketed $54 million with a local businessman. If some bank managers dare to sneak away with cash, it is hard to require credit officers to issue loans and ration credit with prudence regard for bank profits, since it is much easier for them to arrange credits based on friendship or bribery. It is clear that some Chinese bankers were not disciplined and corporate governance of these banks was rather weak.

Table 1. The Chinese Financial System and Non-performing Loans (%).

	2001	2002	2003	2004	2005	2006 e
Equity issuance	7.6	4.0	3.9	5.2	6.0	5.6
Corporate bonds	0.9	1.4	1.0	1.1	6.4	6.1
Government bonds	15.7	14.4	10.0	10.8	9.5	1.4
Bank loans	75.9	80.2	85.1	82.9	78.1	86.8
Big 4 bank asset		60.1	58.0	53.6	52.5	52.2
NPL Ratio		26.2	20.4	15.6	10.5	9.3

Source : China Banking Regulation Commission. Big 4 include Agriculture Bank of China.

Banks have been the governments' ATM for a long time…

Meanwhile, as the owner or the controlling shareholder, the Chinese government pushed these banks to keep lending to inefficient state-owned enterprises for policy reasons, even if these firms were not able to repay the loans. For political reasons, the government is reluctant to allow state-owned enterprises to be liquidated or employees to be dismissed. These banks are subject to political directives. With ongoing political intervention, bankers can easily assert a political excuse for their mistakes or misdeeds when they lend to friends or extend credits that become new non-performing loans. Besides, bankers tend to be evaluated using political rather than professional criteria, making effective corporate governance more difficult. There is definitely cause for investor concern when investing in these Chinese banks.

Yet the Chinese banking market remains overly lucrative

However, the market is not irrational in its enthusiasm for Chinese banks, because the banking market in China is so huge and potentially lucrative. The current Chinese domestic saving rate is as high as 46%[1], but there are no competitive interest rates, since the government not the market sets rates. The Chinese banking authority imposes imperative caps on various deposit rates and floors on different lending rates, guaranteeing a large interest rate spread. For instance, the cap on the benchmark one-year deposit rate is 2.52%[2], while the floor for the one-year lending rate is slightly over 6%, allowing banks and those institutions that loan money a 3.5% interest spread. Bank profitability is safeguarded with these de facto regulatory rents. Behind the percentage figures of table 1, there are US$1.7 trillion of personal deposits and US$ 1.2 trillion of corporate deposits in Chinese banks, which makes the interest spread a huge source of profit. Indeed, more than 90% profits of the state-owned banks come from this spread. It is thus no surprise that Goldman Sachs purchased 5 percent of Industrial and Commercial Bank of China, with the condition of being locked up for years.[3]

Therefore, these Chinese banks can be both a honey pot and a plague. Where it goes depends on the changes made to these banks. In order to go public overseas, the big Chinese banks had to be seriously restructured. Fortunately, this not only dressed up the balance sheets, but also about brought considerable structural changes.

Table 2. Restructuring Measures of the Big Three Chinese Banks.

	Restructuring Measures and Costs Implemented by the Government	USD bn
1	Recapitalization with RMB 270bn of special government bonds	34.6
2	RMB 1.4tn NPL transfer in 1999. At a 20 percent net cash recovery ratio, this should result in a loss of 80 percent, or RMB 1.12tn.	153.8
3	US$60bn foreign exchange capital injection is worth RMB 496bn at the strike price of RMB 8.27/US$1. 496	63.6
4	The Ministry of Finance wrote off its equity of RMB 320bn in CCB and BoC, and RMB 50bn in ICBC. A loan loss of RMB246 is shelved under an ICBC receivable account to be funded by the Ministry of Finance in installments.	79.0
5	The PBC bore the RMB 400bn loss related to the carving out of the doubtful loans at CCB, BoC and ICBC in2004 and 2005.	51.3
6	RMB 35bn recapitalization of Bank of Communications in 2004.	4.5
7	Foreign investors took equity stakes or purchased new shares at a premium. The premium is conservatively estimated at RMB 30bn.	3.8
8	RMB 440bn for RCC and RMB 36bn for city commercial banks.	64.1
9	RMB 270bn spent by bank customers over the past 5 years, and RMB 150bn in pre-provision net earnings based on forbearance in 2003 and 2004. It is assumed that there is an overlap of RMB 100bn between the two.	44.9
10	Low-yielding bank subordinated debt (assuming free lunch).	-
Total		**518.8**

Source: *China & World Economy* , 2006.

IPO improves information disclosure and corporate governance practices, and brings strategic partners into the scene

The Big Three (BoC, CCB, ICBC) went public on the Hong Kong Stock Exchange and thus had to follow relatively strict (particularly for the banking industry) listing rules. Furthermore, to succeed as IPOs, these banks had to improve information disclosure, install governance mechanisms and bring in strategic partners. Compliance with disclosure rules of the stock exchange and dynamic market monitoring made these banks more transparent. Actually, most of the banks' problems discussed above can be resolved or at least controlled, and being under a spotlight will help. Meanwhile, the banks have to assemble shareholder meetings, set up board of directors, and invite independent directors. Besides these, there were block transfers to international strategic investors before going public (see table 3). Although priced below the public offerings, these shares purchased by international strategic investors have to be locked up for at least three years. In any case, these big investors cannot allow their equity investment to be squandered or embezzled; they likely will actively monitor the behavior of bank managers and prevent the controlling government shareholder from politically intervening to a large extent. Consequently, small investors will be protected and motivated to monitor the banks, while partial privatization via oversea listing can significantly improve the banks' corporate governance.

The success story of Bank of China Hong Kong

The fundamental changes that oversea listings may bring to a Chinese bank can be illustrated by the case of Bank of China Hong Kong (BoC HK), the Hong Kong branch of BoC, which was independently listed in July 2002. Although the Chinese government remained the controlling shareholder, BoC HK had to invite several independent directors and subject itself to significant market discipline. When the misconducts of Mr. Liu Jinbao, the former CEO of BoC HK, were exposed, the board of directors quickly disclosed related information to the market and dismissed Mr. Liu. Later, other senior managers were also replaced with new recruits from the global market hired under an open process; in the past, top managers were always hand picked by Beijing. The management team of this bank has gradually become institutionalized and internationalized, which helps prevent corruption and political intervention. After establishing good corporate governance structures and appointing professional bankers as managers, the profitability of BoC HK has steadily increased and the non-performing loan ratio was reduced sharply, which has been sustainable thus far (see table 4). As for return on assets and the price to earnings ratio, BoC HK has caught up with the levels of international renowned banks, like HSBC, though BoC HK operates in the competitive environment of Hong Kong rather than the protected domestic Chinese market.

Table 3. International Strategic Investors and their Investments.

State-owned Banks	International Strategic Investors	Investment (USD mil)	Shareholding %
Bank of China	Royal Bank of Scotland, Merrill Lynch, Li Ka-shing, Temasek, UBS, ADB	5,220	16.80%
China Construction Bank	Bank of America, Temasek	3,996	14.10%
Industrial & Commercial Bank of China	Goldman Sachs, Allianz, American Express	3,660	10.00%

Table 4. Corporate Performance of Bank of China Hong Kong by Year.

	2000	2001	2002	2003	2004	2005
Return to Total Assets %	0.63	0.36	0.94	1.08	1.56	1.64
Non-performing Loan Ratio %	10.19	10.99	7.99	5.78	2.95	1.28
Return on Equity %		7.31	12.52	13.62	18.58	16.99
Capital Adequacy Ratio %		14.38	13.99	15.11	16.14	
Earning per Share HK$	0.477	0.262	0.642	0.753	1.132	1.276

Source : Annual reports of Bank of China Hong Kong.

The past success of BoC HK suggests that Chinese banks are problematic, but these problems can be sorted out by installing good corporate governance. Partial privatization brings in multiple investors and oversea listing leads to monitoring by international investors. Successfully transforming corporate governance will make these Chinese banks a land of potential, though much depends on the Chinese government's determination of and its commitment to respect market rules.

Notes

[1] China's present high saving rate is correlated to many factors, such as traditional Chinese culture, social structure and family concept. However, an important reason why ordinary people are reluctant to consume lies in the unsound social security system.

[2] When inflation is taken into account, real interest rates for depositors stand at roughly minus 3%.

[3] Before public offerings, as a strategic investor, Goldman Sachs spent $2.6 billion for 5 percent of ICBC. Goldman thus has already tripled its money, based on the current share price of ICBC. In addition, Goldman Sachs promised to provide training to the Chinese bankers.

The PB Index

Performance Analysis

Overview

The PB Index tracks the performance of shares of privatized companies that are listed for trading in domestic stock markets of the enlarged European Union.

The PB Index is capitalization weighted, and denominated in Euro. It is restricted to ordinary shares of privatized companies trading in the stock exchanges of the European Union, including the ten new accession countries.

It is subject to a quarterly review by the PB Index Administrator, who ensures the overall consistency with the purposes of the Index. Index maintenance implements the adjustment for company additions and deletions and stock price adjustments due to corporate actions (including dividends) and merger and acquisition (M&A) activity.

The PB Index maintenance rules try to take into account for M&A operations which may affect the risk and return profile of privatized companies. Particularly, the privatized company's share price is replaced by the one of the acquiror *(a)* if the acquiror is a European company listed in a stock market of the enlarged European Union and *(b)* if the acquiror's market capitalization is not more than double of the one of the target. The first condition avoids to include in the PB Index non European stocks exposed to different systemic risk. The second is based on the assumption that in case of M&A the idiosyncratic factors affecting privatized companies spill over only if the private acquiring company is comparable in size.

Following these rules, a Composite Index, two regional sub-indexes (one including EU15 and one the ten new accession countries) are constructed, together with five sector sub-indexes (Banking, Industrial, Oil & Gas, Utilities, and Telecom).

As of January 2006, the PB Composite Index includes 258 stocks. The two regional indexes include 188 companies of EU15 countries and 70 companies of the ten new accession countries of Eastern Europe. The five sector sub-indexes Banking, Industrial, Oil & Gas, Telecom and Utilities, include 37, 39, 14, 25, and 47 stocks, respectively (see Table 1). This new release of the PB Index features 7 new stocks, due to six IPOs executed and two additions thanks to newly available data and one delisting.

A more detailed description of the PB Index can be found in the Rulebook (available at www.privatizationbarometer.net/site/rulebook.pdf).

Analysis

In this section, we briefly describe the return and risk characteristics of privatized companies over the short and the medium run, up to three years.

Figure 1 refers to the PB Composite Index, which includes the whole set of privatized companies for which we track the performance. The figure shows that, had one invested €100 mil in this index in January 2003, after three years the investment would be worth €165 mil. The cumulative return of the PB Composite is now as high as 64.7 percent (Table 2).

Overall, the two broader indexes, namely the PB Composite and the PB Old Europe have underperformed the (European) Dow Jones STOXX Total Market Index (TMI), that we use as benchmark. Over the last year, these two indexes lost 4.1 and 4.9, respectively. However, on a three years basis, the PB Composite yielded (annualized) excess return slightly less then 1 percent. Not surprisingly, the PB Old Europe follow closely the Composite (Table 3).

In previous analyses, we pointed out a similar behavior of the PB New Europe and its benchmark (i.e. the Dow Jones EU Enlarged TMI) and tentatively explained it in terms a high fraction of overlapping capitalization between these two indexes. Surprisingly, we find negative excess returns in the PB New Europe, especially over the last semester.

Our broader PB indexes have been severely hit by strong underperformance of large aerospace and defense such as EADS Group, Dassault, Thomson, which burnt on average almost 20 percent of the market capitalization over the year. A second driver is lasting decline of the telecommunication sector, especially in the fixed line business dominated by former state monopolies.

The strong overperformance of PB Banking Index documented in previous analysis is confirmed. Privatized banks gained a 6.9 percent excess returns on a yearly basis relative to the Dow Jones STOXX Banking. A top driver of this strong performance has been Bankgesellschaft Berlin, which under the pressure of the aggressive bid by DSGV has gained a stellar 157 percent over the year. BANIF and Banco BPI confirm the appeal of the heavily restructured Portuguese banking system, which had a great bearing on the sector rally. In Italy, a more market oriented regulatory environment in Italian banking sector has fostered the merger between Intesa and San Paolo, creating one of the largest banking groups, which yielded more the 30 percent over the year (Table 3).

We also report some overperformance of the PB Utilities Index, which yielded excess returns of 4 percent on a yearly basis. A significant part of this gain is attributable to the high returns of EdF, one the largest companies include in our indexes, mainly driven by the announcements of future tariff liberalization in the electricity business. Other drivers of the high reported gains in the electricity sectors has been the take-over bids launched on the Spanish Endesa, which is likely to see the light soon, and on the French Suez, which gained 60 and 47 percent on a yearly basis, respectively.

In what follows, we briefly analyze the risk-adjusted performance yielded by our PB Indexes by use of the conventional Sharpe ratio, given by the differential return of our index relative to a risk-free investment (namely, the 3-month Euro Interbank Offered Rate) divided by the standard deviation of the differential return. The Sharpe ratio has also been computed for our benchmarks, in order to gauge the differential risk-adjusted performance. We have also computed the Information ratio, given by the differential return relative to its benchmark divided by the so called tracking-error volatility (i.e. the standard deviation of the excess returns). While the Sharpe ratio provides a measure of return per unit of total risk, the Information ratio provides a measure of active risk and hence of relative risk-adjusted performance.

We calculate these ratios for the three-year period, which is the conventional time-horizon used by asset managers and investment consultants.

Over the 36-month period, four PB Indexes - the PB Composite, Old Europe, Banking and Utilities - show higher Sharpe ratios with respect to benchmarks. The more pronounced differences are found for the PB Banking and PB Utilities (Table 7).

The analysis of the Information ratio confirms the relative risk-adjusted performance for a highly diversified portfolio of privatized firms. The Information ratio of the PB Composite Index is 0.16, indicating approximately 20 basis points of out performance relative to the benchmark Dow Jones STOXX TMI for every 120 basis points of (active) risk (Table 8). The PB Utilities and especially Banking indexes report the highest the information ratios, 0.65 and 1.6, respectively.

As customarily, we have estimated a conventional Capital Asset Pricing Model (CAPM), where excess returns over the risk free asset are regressed against a market risk factor and sector excess returns. The PB Banking and PB Utilities Index regressions yield intercepts which are statistically different from zero. These intercepts are the conventional Jensen's alpha, a widely used measure of over performance over large and broadly diversified portfolios. Our estimates based on daily data for these two indexes yield an alpha of 3 and 2 basis points, respectively (Table 9). A back of the envelope calculation suggests that a passive investment in a fund based on the PB Banking index gained approximately 7 percent excess returns on an annual basis with respect to its sector benchmark.

Table 1. PB Indexes Constituents (as of 29/12/2006)

PB Indexes	# of Constituents	Old Europe	% Old Europe	New Europe	% New Europe
Composite	258	188	72.87%	70	27.13%
Banking	37	28	75.68%	9	24.32%
Industrial	39	35	89.74%	4	10.26%
Oil & Gas	14	10	71.43%	4	28.57%
Telecom	25	18	72.00%	7	28.00%
Utilities	47	41	87.23%	6	12.77%

Source: Elaborations on *Datastream.*

Table 2. PB Indexes Returns

PB Indexes	Value as of 29/12/2006	3 Months	1 Year	2 Years	3 Years
Composite	165.312	9.057%	14.190%	39.924%	65.312%
Old EU	163.983	8.946%	13.047%	40.246%	63.983%
New EU	264.320	19.036%	22.782%	73.049%	164.320%
Banking	202.136	5.132%	25.243%	71.727%	102.136%
Industrial	175.315	9.243%	8.977%	45.193%	75.315%
Oil & Gas	153.045	4.577%	0.091%	31.984%	53.045%
Telecom	124.358	12.885%	10.175%	5.825%	24.358%
Utilities	227.109	14.455%	39.432%	73.404%	127.109%

Note: The base date is the 29/12/2003. Return indicates the cumulative % increase/decrease of the index.
Source: Elaborations on *Datastream.*

Table 3. PB Indexes Average Excess Returns

PB Indexes	Benchmarks	3 Months	1 Year	2 Years	3 Years
Composite	DJ Stoxx TMI	10.123%	-3.793%	-2.639%	0.938%
Old EU	DJ Stoxx TMI	9.423%	-4.934%	-2.455%	0.618%
New EU	DJ Stoxx EU Enlgd TMI	-3.894%	-6.561%	-5.073%	-2.905%
Banking	DJ Stoxx Banking	0.562%	6.901%	11.051%	9.693%
Industrial	DJ Stoxx Indl Goods&Serv	-15.505%	-15.512%	-8.284%	-1.894%
Oil & Gas	DJ Stoxx Oil & Gas	2.580%	-4.233%	-1.479%	-0.001%
Telecom	DJ Stoxx Telecom	-9.503%	-5.765%	-3.749%	-1.111%
Utilities	DJ Stoxx Utilities	27.000%	4.065%	0.735%	2.626%

Note: The base date is the 29/12/2003. Average excess return indicates the historic average differential return of the index to its respective benchmark. All values are annualized.
Source: Elaborations on *Datastream.*

Figure 1. Performance of the PB Indexes

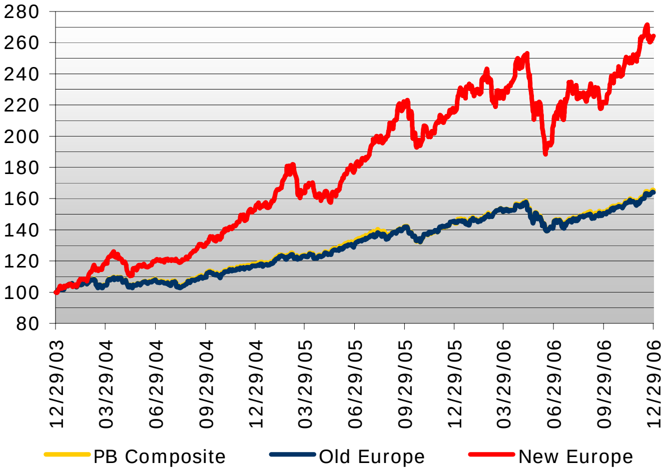


Figure 4. Cumulative Excess Returns of the PB Indexes

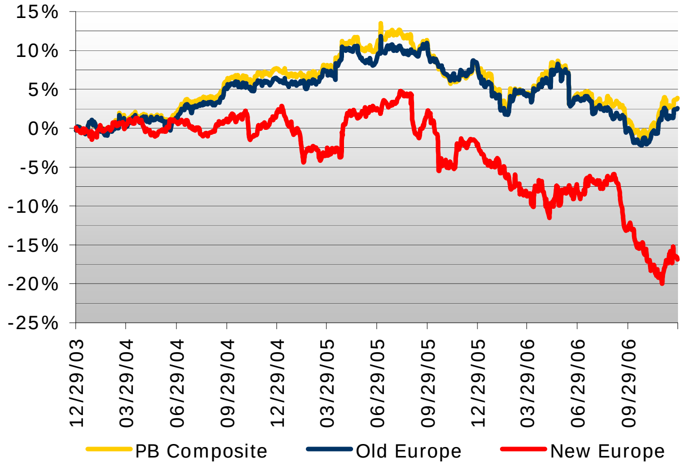


Figure 2. Performance of the PB Indexes

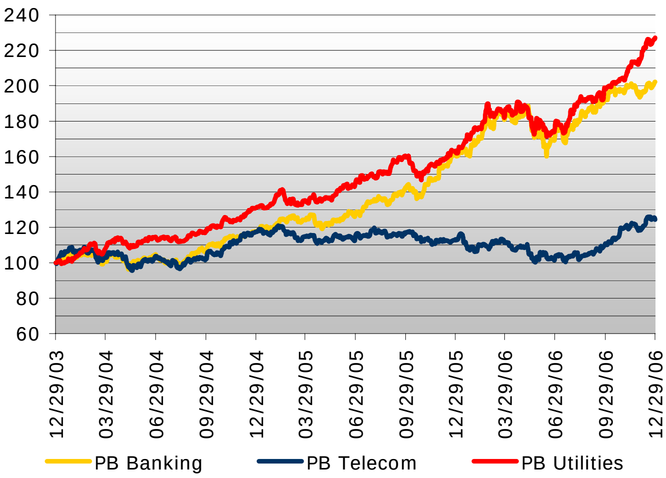


Figure 5. Cumulative Excess Returns of the PB Indexes

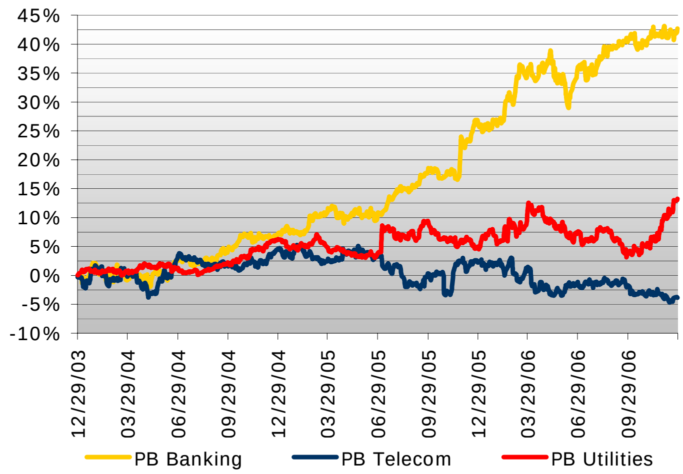


Figure 3. Performance of the PB Indexes

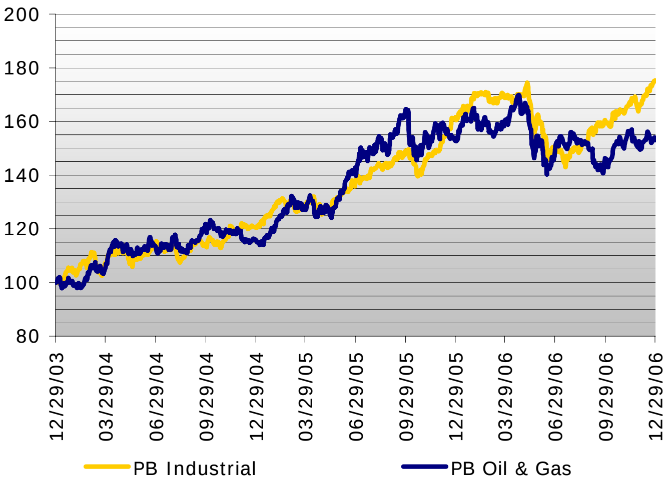


Figure 6. Cumulative Excess Returns of the PB Indexes

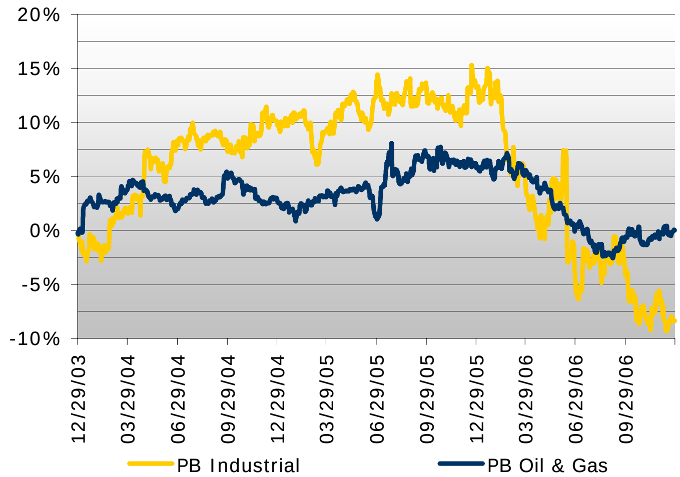


Table 4. PB Index TOP & WORST 10 Performers

OLD EUROPE

	TOP 10 Performers					*WORST 10 Performers*			
	Company	**Nation**	**Value as of 29/12/06**	**1 Year Change (%)**		**Company**	**Nation**	**Value as of 29/12/06**	**1 Year Change (%)**
1	Bankgesellschaft Berlin AG	Germany	7.96	157.61%	**1**	TDC	Denmark	28.57	-43.54%
2	Outokumpu	Finland	29.66	135.21%	**2**	Bull	France	6.07	-37.74%
3	Salzgitter	Germany	99.70	117.92%	**3**	Pages Jaunes	France	15.07	-31.75%
4	Arcelor	France	43.10	103.88%	**4**	Agric. Bank of Greece	Greece	3.90	-21.53%
5	Voestalpine AG	Austria	42.77	100.89%	**5**	Tietonator	Sweden	24.44	-21.06%
6	BANIF	Portugal	5.30	96.30%	**6**	EADS	France	26.10	-19.86%
7	Gescartao	Portugal	24.50	96.16%	**7**	Thomson	France	14.81	-17.72%
8	Volkswagen	Germany	85.96	90.73%	**8**	Dassault Systems	France	40.20	-16.02%
9	Corus Group	UK	7.87	82.18%	**9**	OMV	Austria	42.99	-13.15%
10	SSAB	Sweden	18.01	75.54%	**10**	General Hellenic Bank	Greece	8.80	-12.00%

NEW EUROPE

	TOP 10 Performers					*WORST 10 Performers*			
	Company	**Nation**	**Value as of 29/12/06**	**1 Year Change (%)**		**Company**	**Nation**	**Value as of 29/12/06**	**1 Year Change (%)**
1	Kopex	Poland	8.10	415.92%	**1**	Prochnik	Poland	0.22	-47.62%
2	Mostostal Warszawa	Poland	10.71	361.64%	**2**	Philip Morris CR	Czech Rep.	393.83	-37.17%
3	Hutmen	Poland	7.52	265.05%	**3**	Krosno	Poland	1.43	-30.24%
4	Elektrobudowa	Poland	27.94	191.04%	**4**	PKN Orlen	Poland	12.46	-23.61%
5	Kruszwica	Poland	19.69	187.45%	**5**	LASCO	Latvia	1.54	-16.76%
6	Impexmetal	Poland	44.92	147.49%	**6**	Police	Poland	1.77	-15.31%
7	Vistula	Poland	23.50	142.27%	**7**	Ventspils Nafta	Latvia	3.37	-12.01%
8	Zelmer	Poland	14.89	142.11%	**8**	Komercni Banka	Czech Rep.	112.59	-5.24%
9	Mostostal - Export	Poland	0.81	138.24%	**9**	Cesky Telecom	Czech Rep.	17.29	-4.48%
10	Bytom	Poland	5.79	84.98%	**10**	Bank of Valletta	Malta	8.62	0.00%

Source: Elaborations on *Datastream.*

Table 5. PB Index Old Europe Sectorial Top Performers

		Company	Nation	Value as of 29/12/06	1 Year Change (%)
Banking	**1**	Bankgesellschaft Berlin AG	Germany	7.96	157.61%
	2	BANIF	Portugal	5.30	96.30%
	3	Banco BPI	Portugal	5.91	53.51%
Industrial	**1**	Thessaloniki Port Authority	Greece	17.00	62.84%
	2	Metso	Finland	38.24	62.59%
	3	Assocoated British Ports Hdg	United Kingdom	13.49	56.86%
Oil & Gas	**1**	Saipem	Italy	19.74	42.22%
	2	British Gas	United Kingdom	10.29	22.35%
	3	Eni	Italy	25.48	8.38%
Telecom	**1**	British Telecom	United Kingdom	4.47	37.96%
	2	TeliaSonera	Finland	6.23	35.14%
	3	Sirti	Italy	2.13	34.04%
Utilities	**1**	ACEA	Italy	14.53	72.87%
	2	Electricité de France	France	55.20	71.00%
	3	International Power	United Kingdom	5.67	61.54%

Table 6. PB Index Old Europe Sectorial Worst Performers

		Company	Nation	Value as of 29/12/06	1 Year Change (%)
Banking	**1**	Banco Totta Acores	Portugal	36.000	0.00%
	2	Agricultural Bank of Greece	Greece	3.900	-21.53%
	3	General Hellenic Bank	Greece	8.800	-12.00%
Industrial	**1**	EADS	France	26.100	-19.86%
	2	AEA Technology	United Kingdom	1.450	-11.59%
	3	Eniro	Sweden	10.030	-4.84%
Oil & Gas	**1**	OMV	Austria	42.990	-13.15%
	2	Hellenic Petroleum	Greece	10.440	-9.06%
	3	British Petroleum	United Kingdom	8.420	-7.27%
Telecom	**1**	TDC	Denmark	28.570	-43.54%
	2	Telecom Italia	Italy	2.290	-8.03%
	3	Deutsche Telekom	Germany	13.890	-1.56%
Utilities	**1**	META	Italy	2.880	-2.37%
	2	Water Supply & Sewerage Systems	Greece	7.220	-0.28%
	3	Public Power Corp	Greece	19.200	3.23%

Source: Elaborations on *Datastream.*

Table 7. PB Indexes Sharpe Ratios

Indexes	PB Index	Benchmark	PB Index	Benchmark	PB Index	Benchmark
	1 Year		*2 Years*		*3 Years*	
Composite	0.985	1.184	1.547	1.667	1.504	1.329
Old EU	0.890	1.184	1.558	1.667	1.463	1.329
New EU	0.885	1.258	1.380	1.721	1.953	2.232
Banking	1.454	1.114	2.107	1.451	1.810	1.180
Industrial	0.473	1.298	1.607	1.921	1.501	1.476
Oil & Gas	-0.182	0.076	0.782	0.877	0.807	0.820
Telecom	0.548	0.858	0.037	0.304	0.402	0.443
Utilities	2.845	2.484	2.449	2.287	2.583	2.231

Note: Sharpe Ratio indicates the historic average differential return of the index over a risk-free asset (Euribor Interbank Offered Rate 3m) per unit of historic variability of the differential return.
Source: Elaborations on *Datastream.*

Table 8. PB Indexes Information Ratios

PB Indexes	1 Year	2 Years	3 Years
Composite	-0.710	-0.518	0.194
Old EU	-0.913	-0.486	0.128
New EU	-1.559	-1.130	-0.670
Banking	1.265	1.842	1.601
Industrial	-1.720	-1.094	-0.258
Oil & Gas	-1.412	-0.420	0.000
Telecom	-0.931	-0.574	-0.168
Utilities	0.883	0.166	0.648

Note: Information Ratio indicates the historic average differential return of the index to its respective benchmark per unit of historic variability of the differential return.
Source: Elaborations on *Datastream.*

Table 9. PB Indexes Jensen Alphas

PB Indexes	Jensen α	β	R-squared
Composite	0.0001%	0.848	81.46%
	(1.05)	(58.28)	
Composite*	0.0001%	0.462	83.09%
	(0.74)	(4.80)	
Old EU	0.0001%	0.857	81.78%
	(0.94)	(58.91)	
Old EU*	0.0001%	0.452	83.75%
	(0.59)	(4.74)	
New EU	-0.0001%	1.029	94.56%
	-(1.14)	(115.92)	
Banking	0.0003%	0.973	79.48%
	(2.42)	(54.72)	
Industrial	0.0001%	0.753	71.22%
	(0.77)	(43.75)	
Oil & Gas	0.0000%	0.986	95.09%
	(0.10)	(122.41)	
Telecom	0.0000%	0.790	78.15%
	(0.05)	(52.59)	
Utilities	0.0002%	0.894	88.36%
	(1.98)	(76.62)	

* Market sectorial controls included.
Source: Elaborations on *Datastream.*

Selected News

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DENMARK

2006-10-26 - **Danish Finance Ministry Plans Listing Of DONG In 2H2007**

COPENHAGEN (Dow Jones)--The Danish finance ministry said it has started preparations to list **DONG Energy A/S** on the Copenhagen stock exchange in the second half of 2007. The ministry will look to sell part of its holding in DONG, but will retain the majority stake in the company. The partial listing was originally aimed for 2006, but was delayed pending E.U. Commission approval of a fusion between DONG and other Danish energy companies. The finance ministry has previously told that the flotation in the offering could be about 28% of the total share capital in the company. DONG Energy was formed by the fusion of DONG, Elsam, Nesa and Energy E2, which started in 2004 and was completed in March, when the Commission approved the final acquisitions. Analysts have valued the company at around DKK60 billion to DKK64 billion ($10.5 to $11.2 billion).

FRANCE

2006-12-19 - **DCN Board Approves Naval Tie-Up With Thales**

PARIS (Dow Jones)--**DCN**, the French State-owned naval shipyard, said its board of directors has approved a tie-up with Thales SA, the defense electronics group. The deal, which has been under discussion for the past several months, will see Thales take a 25% stake in DCN in exchange for some of DCN's naval assets. The French State will retain a 75% share in DCN. In its statement, DCN said the terms and conditions of the tie-up are now being finalized.

GERMANY

2006-07-11 - **German Air-Traffic Control Head Sees Privatization In 2007**

LANGEN, Germany (Dow Jones)--The privatization of Germany's air-traffic control agency **Deutsche Flugsicherung GmbH**, or DFS, will likely be delayed until 2007, Chief Executive Dieter Kaden said at the company's annual press conference. The entire transaction will take more than three months, adding that the sale process will be started in late fall. Kaden also said he expects potential buyers will be presented around that time. The German government, which owns 100% of DFS, initially planned to float the company by the end of the year, retaining ownership of just over 25% of shares.

2006-10-25 - **German State Plans To Sell Real Estate Company**

FRANKFURT (Dow Jones)--Germany's North Rhine-Westphalia State plans to sell off its real estate company, **Landesentwicklungsgesellschaft**, or LEG, for more than EUR2.5 billion, reports Handelsblatt, citing State Finance Minister Helmut Linssen. According to the newspaper, the State wants to privatize LEG, which has a portfolio of around 100,000 apartments, by early 2008 at the latest, and sale proceeds will be used to amortize LEG debts worth EUR2.5 billion, while any extra money will be put into an investment fund or used to lower general State debt.

2006-12-12 - **KfW Plans to Raise About EUR55 Billion In Capital Markets In 2007**

FRANKFURT (Dow Jones)--Germany's KfW Banking Group is planning to raise around EUR55 billion in capital markets next year to fund its activities. "In 2007, KfW expects funding needs to amount to around EUR55 billion," Guenther Braeunig, a KfW board member in charge of capital market activities, said at a press conference. In light of the bank's sale of shares in **Deutsche Telekom AG** and **Deutsche Post AG**, Braeunig said: "Next year, we'll again look at sales opportunities while maintaining our philosophy of placing shares without upsetting the market and when appropriate capital market windows open up." KfW is helping the German government privatize the two companies. The government sells shares to the group, which, when the conditions allow, places them in the market. At present, KfW still holds 16.9% of Deutsche Telekom shares and 35.4% of Deutsche Post. The German government still has 14.8% in Deutsche Telekom shares. Braeunig didn't rule out that the government could sell further Deutsche Telekom shares to the banking group next year.

2006-12-13 - **Six Bidders On Short List For Hamburg Port**

FRANKFURT (Dow Jones)--Six bidders have been selected in the shortlist for Hamburg's port operator **Hamburger Hafen und Logistik AG**. According to the newspaper Frankfurter Allgemeine Zeitung, the shortlist comprises both strategic investors, including Deutsche Bahn AG and Dubai Ports World, as well as financial investors, said to include private equity investor 3i Group PLC. HHLA management prefers a public listing of the company, in which no shares with voting rights would be listed. The Hamburg municipality wants to sell its 49.9% stake in the port.

2006-12-20 - **Landesbank Berlin Attracts Over 12 Possible Buyers**

FRANKFURT (Dow Jones)--**Landesbank Berlin Holding AG** (operating until August 2006 under the name of Bankgesellschaft Berlin) has attracted the interest of more than a dozen possible buyers, according to the head of UBS AG's Investment Banking operations in Germany, Herman Prelle. UBS has been mandated by the City of Berlin last August as an adviser in the upcoming disposal of the City's 80.95% stake in the Berlin bank. According to press reports, the price is likely to be in the region of EUR6-EUR8 billion and the interest is also evident in the recent share price performance. "The process will start in the first quarter of 2007, with a view to close before the summer break," head of M&A within the financial services sector at UBS, Florian von Hardenberg affirmed. The M&A team at the bank explained that both a sale of the stake, as well as a secondary public offering, will be considered. Already 7% of the shares are in free float, while 10% is held by Dekabank and 2% by Gothaer Holding. "We see a good chance of this being the largest public offering next year," Prelle said. Von Hardenberg added that an official announcement of the disposal will probably be made in January, after which interested parties are invited to show their interest.

The background to the sale is that the bank nearly collapsed in 2001 when a revaluation of its real estate-related liabilities erased its entire capital. Subsequently, the European Commission approved a EUR23 billion bailout by the City of Berlin, under the condition that the city sell its stake by 2007.

2007-01-08 - **Regional State Mulls WestLB Stake Sale**

FRANKFURT (Dow Jones)--The federal State of North Rhine-Westphalia might sell its stake in federal State bank **WestLB**, daily Handelsblatt reported, citing the State's financial minister Helmut Linssen. North Rhine-Westphalia would sell the bank after the restructuring is completed, possibly to a large European bank. "We are not in a hurry. The price for the bank will increase with its performance", Linssen told the paper. Experts estimate the bank, in which North Rhine-Westphalia holds just under 38%, is worth between EUR7 billion and EUR8 billion, according to Handelsblatt.

2007-01-29 - **RAG IPO Expected In Autumn 2007 Following Politicians' Coal Compromise**

FRANKFURT (AFX)--**RAG AG** could be listed in autumn 2007 following an agreement between the Social Democrats (SPD) and the Christian Democrats (CDU) regarding the future of coal mining in Germany that clears the path for an IPO of the coal-producing company, reported Financial Times Deutschland, citing sources. The CDU had originally called for all mines to close by 2018 at the latest, but now the two parties have agreed to postpone the decision until 2012, the newspaper said, adding that the agreement between the two parties is to be signed later today. The German financial daily said that RAG's IPO is expected to raise around EUR5.4 billion, citing an unpublished survey. RAG has said it will use any IPO proceeds to cover decommissioning costs if the government presses ahead with plans to end coal mining during the next decade.

GREECE

2006-10-31 - **Greece To Privatize 38% Of Attica Bank**

ATHENS (Dow Jones)--The Greek government is expected to announce plans early next month to privatize roughly a 38% stake in **Attica Bank**, as part of its 2007 privatization program, financial daily Imerisia reported. The newspaper said French mutual bank Caisse Centrale des Caisses d'Epargne and a local Greek pension fund had expressed interest in the bank.

2007-01-03 - **Greece Eyes Possible Further Listing Of OTE In 2007**

ATHENS (Dow Jones)--Greece may consider listing more shares of local phone giant **Hellenic Telecommunications Organization SA** on the Athens bourse if it fails to find a strategic investor to help manage the company, Finance Minister Giorgios Alogoskoufis affirmed. "We will proceed with trying to find a strategic partner. But if we don't find the right strategic partner, we may proceed with further privatization by listing shares on the market and the management will remain in Greek hands," he said at a news conference. The government, which owns 38.7% of OTE, wants to sell up to a 20% of its holdings in the company as the centerpiece of its EUR1.7 billion privatization plan for 2007. To date, it has insisted on finding a strategic investor - preferably a European company with experience in the telecom sector - and that the company will have a major say in managing OTE. Regarding the government's overall privatization program for this year, Alogoskoufis reaffirmed plans for the further privatization of **Greek Postal Savings Bank SA**, **Bank of Attica SA** and the **Mount Parnes Casino**. The Greek State listed and sold off over a third of Postal Savings Bank in the spring 2006, retaining 65.2 %, and the government is considering selling another 31 %. It holds 77.3% and 38% stakes respectively in the other two banks.

2007-01-31 - **Greece Eyes Placement Of Post Savings Bank By End February**

ATHENS (Dow Jones)--The Greek government is considering placing 15% of **Greek Postal Savings Bank SA** by the end of February as part of its 2007 privatization program, financial daily Imerisia reported. Citing unnamed sources, the newspaper said that the government hopes to raise EUR450 million, depending on market conditions. Last May, Greece sold down a 34.84% stake in the bank through a listing on the Athens stock exchange. The government currently controls 65% of Postal Savings.

ITALY

2006-12-29 - **Italian Government Publishes Alitalia Privatization Details**

MILAN (Dow Jones)--Italy's Economy Ministry published final details for the sale of its controlling stake in struggling flag-carrier airline **Alitalia SpA**. The buyer must acquire at least 30.1% of Alitalia, must guarantee the airline's 18,000 jobs, domestic routes, and the Italian identity of the Alitalia brand, according to the tender document published on the Treasury Web site. Italy has invited bids for at least 30.1% of Alitalia's shares, to be submitted by Jan. 29, 2007. Under Italian law, a buyer of more than 30% of a company must make a public offer to buy out the other shareholders. According to the document, bidders must have a social capital of at least EUR100 million, and must commit to holding their controlling stake for a "sufficient time", until targets they have laid out in an industrial plan for the airline have been met. The ministry reiterated that its selection of a winning bid will depend on the economic content of the bid, and on whether the industrial plan presented by the bidder is judged likely to be successful in "developing and re-launching" the ailing airline. Unions are opposed to Alitalia's privatization and have this week announced a strike for Jan. 19. Italy plans to conclude the Alitalia stake sale within six months, Economy Minister Tommaso Padoa-Schioppa said earlier this month.

2007-01-30 - **Alitalia Draws Interest From 11 Possible Suitors**

MILAN (Dow Jones)--Eleven potential bidders have expressed interest in taking over **Alitalia SpA**, but the government still has a long way to go as it tries to convince potential investors that the state-run carrier can be turned into a profitable investment. Among the bidders that emerged last night: a group led by Management & Capitali SpA, a fund run by financier Carlo De Benedetti, which included hedge fund Cerberus European Investments LLC; private-equity fund Texas Pacific Group Europe LLC, which recently invested in Australian carrier Qantas; the investment-banking arm of Unicredito SpA, Italy's largest bank; and United Kingdom-based Terra Firma Investments Ltd. Carlo Toto, the founder and chairman of Italy's second-largest carrier by passenger traffic, Air One SpA, also expressed interest. The list included six other bidders but not Air France-KLM SA, which confirmed that it wouldn't take part. Italy, which owns 49.9%

of Alitalia, hopes to sell at least a 30.1% stake, which would give the buyer control of the airline and require it, under Italian securities law, to make a cash offer for all outstanding shares. Alitalia has a market value of 1.49 billion euros ($1.92 billion). The nonbinding expressions of interest mark an early victory for the government in its effort to shed Alitalia by setting up the potential for competition among bidders. However, questions remain about how much latitude any potential bidder may have to restructure the airline, which hasn't posted a profitable quarter in more than four years. Some potential buyers are likely to drop out if the government doesn't allow a free hand at running the business, which is likely to include laying off some of Alitalia's 18,000 workers and redesigning the airline's route structure.

PORTUGAL

2006-09-28 - **Portuguese Government Approves IPO Of Up To 19% Of REN**

LISBON (Dow Jones)--The Portuguese government has approved the initial public offering of up to 19% of electricity grid operator **REN**, the government said in a regulatory filing. The timing and pricing of the IPO weren't disclosed, but the Finance Ministry has previously said it would take place in 2006. REN is currently wholly State owned. The flotation is part of a broader restructuring of the country's energy sector. The Portuguese government expects to raise EUR2.4 billion from the sale of various State-held assets through 2006 and 2007.

SPAIN

2006-07-19 - **EU Drops Case Against Spanish Government's "Golden Shares"**

BRUSSELS (Dow Jones)--The European Commission has closed its case against Spain concerning the "golden share" holdings in that country's privatized companies, which enabled the government there to veto takeovers of strategic assets. The Spanish government has notified the commission of measures taken to comply with a European Court of Justice ruling in May 2003 against the legality of the "golden share" mechanism, the commission said. Legal changes approved in Spain have brought its privatization legislation into line with the court's ruling. The government held "golden shares" in companies including power utility Endesa SA, phone company Telefonica SA and oil and energy company Repsol YPF SA.

2006-10-11 - **Spain Sepi Delays Endesa, Iberia, Red Electrica Stake Sales**

MADRID (Dow Jones)--Spanish State-owned holding company Sepi has delayed until 2008 the planned sales of its stakes in electricity firm **Endesa SA**, airline **Iberia Lineas Aereas de Espana SA** and power grid operator **Red Electrica SA**. "Sepi is being cautious with its 2007 budget," said a spokesman, confirming comments made by Sepi Chairman Enrique Martinez Robles to Spain's Congress. Sepi owns a 2.95% stake in Endesa, 20% in Red Electrica and 5.8% in Iberia; the company had originally planned to sell some or all of its stakes in 2006.

SWEDEN

2006-12-14 - **Sweden Government To Sell Stakes In 6 State-Owned Companies**

STOCKHOLM (Dow Jones)-- Sweden's center-right government detailed plans to sell off its share of six companies it wholly or partly owns, and Financial Markets Minister Mats Odell would be responsible for the sale process. Odell said the government plans to sell its 45.3% stake in telecoms company **TeliaSonera AB**, its 19.9% stake in **Nordea Bank AB**, Scandinavia's largest bank by market capitalization, and the government's 6.7% stake in stock-exchange operator **OMX AB**. Wholly-owned companies **V&S Group**, maker of Absolut vodka, property company **Vasakronan**, and mortgage company **SBAB** will also be sold. The new government, which came to power on September 17, 2006 said in October it's looking to sell around SEK150 billion in State assets over the next three years to reduce debt. Thursday's announcement confirmed which assets will be put to the front of the shelf. One surprise omission from the list was the government's 21.4% stake in Scandinavian airline SAS AB. "More analysis is needed for SAS," said Odell. More companies could in the future be included on the list and SAS will likely be one of those, he added. The Swedish government has interests in 55 companies.

UNITED KINGDOM

2006-09-18 - **National Health Service Workers Call Strike Over NHS Logistic Privatization**

LONDON (AP)--Workers angry over the privatization of part of the UK's National Health Service have called a second nationwide strike. The employees of **NHS Logistics**, which delivers goods ranging from bedpans to food to hospitals and doctors' offices across England, will walk out on Sept. 26 for 24 hours. Thursday in the biggest outbreak of industrial unrest in the NHS for almost 20 years. The employees voted to take industrial action after the government confirmed the transfer of their jobs to the German-owned delivery giant DHL. Unison said the 10-year contract is worth GBP3.7 billion.

2007-01-27 - **Consortium Finalizes GBP400 Million Bid For Tote**

LONDON (Dow Jones)-- A horseracing industry consortium finally submitted its GBP400 million bid to buy state-run bookmaking company **Tote** last night, The Independent reports without citing sources. The group is understood to have met a U.K. government valuation, set by PricewaterhouseCoopers, and Tote staff and management are thought to be getting around 20% of equity in the company, the newspaper reports.

CZECH REPUBLIC

2006-09-25 - **Czech Government To Sell Portion Of State's CEZ Shares**

PRAGUE (Dow Jones)-- Czech Finance Minister Vlastimil Tlusty affirmed that the government has approved a plan to sell some of the State's share in power company **CEZ AS**. The plan calls for selling a maximum of 31 billion koruna (about $1.46 billion) worth of CEZ shares to shore up the government's budget in 2007. The Czech State holds a 67.61% stake in the power company. Tlusty

declined to say how many of its CEZ shares the State planned to sell. With its market capitalization of about $20 billion CEZ is one of the largest publicly traded companies in central Europe. The Minister said the State will most likely begin selling its CEZ shares in 2007 and will carry it out in a staggered manner. "Our attention is to move slowly and not to affect the share price," Tlusty told reporters. The government has yet to select a sales adviser and hammer out details of the planned transaction. "We have only decided to launch the sale; no details have been settled yet," Tlusty said.
Later on December 12th, 2006, the Czech Government released some details about CEZ's partial sale. Finance Minister said that "The cabinet approved its intention to sell a minority stake in CEZ, a maximum of 8% needs to be sold to bring down the deficit (to targeted levels)". The sale of an 8% stake in CEZ would generate roughly 30 billion Czech koruna ($1.43 billion).

2006-12-21 - **Czech Airlines Expects CZK42 Million Net Profit In 2007**

PRAGUE (Dow Jones)--Ceske Aerolinie AS, or **CSA**, the Czech flagship airlines, said it will complete the sale of its cargo terminal at the Prague international airport and sell its catering operations in their entirety in 2007 as part of the company's restructuring. Czech Finance Ministry officials said recently that the State would like to launch privatization of the airline as soon as in 2009, but the sale is currently stalled due to the company's string of losses. The Czech government, which controls 91.5% of CSA, aims to return the airline to profit, at which point it is likely to privatize the company.

HUNGARY

2006-07-05 - **Hungary To Sell MAV Cargo, Revamp State Transport Operations**

BUDAPEST (Dow Jones)--Hungary plans to sell State-owned railway freight company **MAV Cargo** within a year as part of its extensive overhaul of the public transport system operation comprising railway and long-distance bus services. "The government decided today on the sale of MAV Cargo. We plan to use the proceeds to pay off (part of) MAV's debts," Finance Minister Koka said after the cabinet's weekly meeting. Koka declined to specify how much in proceeds the government plans to get from the sale of the profitable freight company, which has been separated in accounting and administrative terms from the nearly bankrupt State railway firm MAV Zrt. "We plan to close the transaction within the next 12 months. Initial talks have already started with potential buyers in the industry," Koka said.

2006-08-03 - **Hungary Government To Sell Troubled Farm Company Babolna**

BUDAPEST (Dow Jones)--The Hungarian government will try to sell troubled farm products company **Babolna Zrt**, which is currently fully State-owned, business daily Vilaggazdasag said. The government plans to invite a public tender for the privatization of the company and hopes to rake in 7 billion forints ($32.8 million) from the sale, the paper said.

2006-09-12 - **Hungary Government Calls Tender For The Sale Of Carrier Malev**

BUDAPEST (Dow Jones)--The Hungarian privatization office APV Zrt. called a public tender for the sale of a 99.95% stake in troubled national carrier **Malev**.

The deadline for submitting the bids is November 3, 2006 and APV will invite the chosen bidders to further negotiations. APV expects bidders to commit to raising the company's registered capital, which currently stands at 3.5 billion forints ($16.1 million). Bidders will also have to submit proposals on how they wish to settle Malev's debt that carries a State guarantee. Potential buyers will have to declare whether they wish to maintain Malev's national carrier status, which by law requires that at least 50% plus one vote of the company is in Hungarian, but non-governmental ownership. Bidders will also have to sign a contract that contains certain guarantees regarding the employment of Malev's personnel. Since its return to democracy in 1990, Hungary has repeatedly tried to sell the indebted carrier without any success.

2006-10-12 - **Hungary Government To Sell 40% Of Highway Company AKA In 2006**

BUDAPEST (Dow Jones)--The Hungarian government plans to sell its 40% stake in partly State-owned highway management company **Alfold Kocesszios Autopalya Zrt.** this year, national daily Nepszabadsag says. The owners of the remaining 60% stake in AKA include Bouygues S.A. of France and Strabag AG of Germany. The daily estimates the 40% stake is worth up to 25 billion forints ($117 million).

2006-12-19 - **EU Clears Hochtief, CDPQ To Buy Budapest Airport**

BRUSSELS (Dow Jones)--The European Commission has cleared German construction company Hochtief AG and Canadian investment fund Caisse de Depot et Placement du Quebec, CDPQ, to buy a 75% stake in Budapest's Ferihegy airport from U.K. airport operator BAA PLC. The value of the deal hasn't been disclosed. Hochtief will hold almost 50% of the shares in the consortium through its airport services subsidiary Hochtief Airport. The firm also has stakes in Athens, Sydney, Duesseldorf, Hamburg and Albania's Tirana airport. BAA paid about EUR1.8 billion for the Budapest airport stake last year in Hungary's biggest-ever privatization deal, outbidding a consortium led by Hochtief. The sale included a 75-year operating license. The takeover was cleared under the commission's simplified procedure. This clears deals automatically after one month if no third party lodges a complaint.

2006-10-31 - **Hungary Government To Sell 50% FHB Stake To Financial Company Via Tender**

BUDAPEST (Dow Jones)--The Hungarian government plans to launch a tender to sell a 50% plus one-vote stake in part State-owned mortgage bank **FHB Jelzalogbank Nyrt**. to a financial company. The State owns 54.1% of FHB. Of this, 50% plus one-vote is series "A" stock and the remaining 4.1% is made up of series "B" shares. Series "A" shares were listed on the Budapest Stock Exchange in 2003. The announcement on the sale was made by Hungary's Finance Ministry. FHB is a significant player on Hungary's mortgage market. At the end of June, institutional investors - domestic banks - held 8% of FHB's series "B" shares. Of the series "A" shares, 37.9% were publicly traded on the stock exchange. In the first half of this year, FHB's net profit totaled 3.75 billion forints ($18.2 million), down from HUF4.53 billion a year earlier, due to falling interest margins and higher costs entailed by the company's restructuring plans.

2006-12-27 - **Hungary Government To Fully Sell Highway Management Company**

BUDAPEST (Dow Jones)--The Hungarian government is planning to fully privatize the State-owned highway management company **AAK Zrt.**, national daily Nepszabadsag reported. The privatization would yield revenue of up to 500 billion forints ($2.59 billion), which the State could use to pay back national debt. The State previously said it was looking to sell a minority stake in AAK through the Budapest Stock Exchange.

POLAND

2006-10-05 - **Treasury Favors Go-Slow Privatization Strategy**

WARSAW (Dow Jones)--Poland has no plans to sell further shares in big listed companies in which the State retains significant stakes, Deputy Treasury Minister Ireneusz Dabrowski told the daily Gazeta Prawna in an interview. "Companies like KGHM Polska Miedz, PKN Orlen, and Grupa Lotos are like hens laying golden eggs in the form of very high dividends, so it doesn't make sense to sell these assets too quickly," Dabrowski said. He added that the same principle applied to Poland's power sector, where the government is forming vertically consolidated groups that may consider minority listings on the Warsaw Stock Exchange. "Profits (in the power sector) will be so high that collecting dividends is a better solution than total privatization," he said.

2006-10-24 - **Polish Treasury Ministry Sees 2006 Privatization Revenues At PLN 1 Billion**

WARSAW (Dow Jones)--Poland's Treasury Ministry expects privatizations to generate about one billion zlotys ($335 million) revenue in 2006, Treasury Minister Wojciech Jasinski affirmed. This forecast is considerably lower than the PLN5.5 billion ($1.85 billion) privatization revenue factored into the 2006 budget. During the first nine months of this year, privatizations yielded revenue of just PLN514.5 million ($17.3 million). Jasinski said the privatization revenue could be higher had the ministry gone through with the sale of three power plants: Ostroleka, Kozienice and Dolna Odra. "But first we have to complete their consolidation," Jasinski said. He added that the energy sector is probably the last large privatization project and that the ministry plans to float over 40% of energy holding **Poludniowy Koncern Energetyczny**, or **PKN**, in 2007. The sale might generate "billions of zlotys," Jasinski said.

ROMANIA

2007-01-23 - **Romania To Sell Electrica Branches In 2H2007 - Mediafax**

BUCHAREST (Dow Jones)-- Romania's privatization authority, or AVAS, plans to sell the last three remaining branches of state-owned power grid **Electrica SA** in the second half of the year, after their supply and distribution operations are separated according to E.U. regulations, news agency Mediafax reported, citing AVAS President Teodor Atanasiu. "Romanian and European laws stipulate that we must split the branches' supply and distribution operations by June 30. We will privatize them immediately after the splitting," Atanasiu said at a press conference. Electrica General Director Nicolae Coroiu said Electrica would split the supply and distribution operations of four of its regional branches by the end of June, including those of supplier Electrica Muntenia Sud, which is currently being privatized. Electrica has so far sold four of its eight branches. Enel bought two of Electrica's branches, namely Electrica Banat and Electrica Dobrogea, while Electrica Oltenia and Electrica Moldova were bought by Czech CEZ AS and German firm E.ON AG, respectively. Electrica still owns Electrica Muntenia Sud, Muntenia Nord, Transilvania Nord and Transilvania Sud.

SLOVAKIA

2006-08-30 - **Slovakia To Allow Sale Of 2nd Largest Airport, But Not 1st**

BRATISLAVA, Slovakia (AP)--The government will allow the multimillion-dollar sale of Slovakia's second-busiest airport to an Austrian-led consortium, though it has blocked privatization of the busiest airport, Prime Minister Robert Fico said Wednesday. Slovak regulators earlier this month approved selling control in the **Kosice international airport** in eastern Slovakia to the TwoOne consortium led by Flughafen Wien AG for $75 millionThe Fico's government canceled the privatization of the country's biggest airport, in Bratislava, to the TwoOne consortium. The TwoOne consortium, which also includes Slovak private equity firm Penta and Austria's Raiffeisen Zentralbank Oesterreich AG, had initially hoped to buy control in both airports for about $147 million - a deal approved in February by Slovakia's previous government. The TwoOne consortium has said it plans to appeal to an arbitration court in Paris against the government's decision to reject its purchase of the **Bratislava airport**.

SLOVENIA

2006-10-02 - **Slovenia Plans To Call Tender for 39% of Its Telco in April 2007**

LJUBLJANA (SeeNews)-- Slovenia plans to call a tender for the sale of 39% of its telecoms company **Telekom Slovenije** to a strategic investor in April next year, an Economy Ministry official said. "I expect the public tender to be called in April 2007 and privatisation to be finished in the autumn of 2007," the director general of the Electronic Communications Directorate at the ministry, Matjaz Jansa, told in a recent interview. "We will choose four bidders to examine the company more closely, to conduct due diligence and set the price," Jansa added. Slovenia's centre-right government adopted in May a plan for the privatisation of the fixed-line and wireless services telecoms company. The plan calls for the sale of up to 39% to a strategic investor and at least 10% are to be offered to Slovenian citizens. The government, which owns 74% of Telekom Slovenije directly and indirectly, will keep a stake of 25% plus one share in the company. Telekom Slovenije floated 6,535,478 shares with a face value of 10,000 tolars each, or 100% of its equity capital, on the Ljubljana Stock Exchange on Monday as a first step in its privatisation. "Only if we do not receive an appropriate offer when selling to a strategic partner, then we will be forced to sell on the bourse and we will have to go to a foreign stock exchange as the Slovenian one is very small but this is a very unlikely scenario," he added. He said that companies from Japan to America had expressed interest in the privatisation of Telekom Slovenije because the company is technologically advanced and at the same time it is relatively small. "The majority of European telecoms operators and financial companies can afford this purchase," Jansa said. "

Table 1. Announced Deals

Date of Announcement	Company Name	Country	Percent for Sale	Method of Sale	Date Expected (as announced)	Rescheduling /Notes
Jan-07	RAG AG	Germany	unspecified	IPO	2007	
Jan-07	Stadtwerke Leipzig GmbH	Germany	49.00	Private Sale	Spring 2007	
Jan-07	WestLB	Germany	38.00	unspecified	unspecified	
Dec-06	SBAB	Sweden	unspecified	unspecified	by 2008	
Dec-06	Vasakronan	Sweden	unspecified	unspecified	by 2008	
Dec-06	Hamburg Port	Germany	49.90	Private Sale	unspecified	
Dec-06	Deutsche Telekom	Germany	unspecified	unspecified	2007	through KfW
Dec-06	Deutsche Post	Germany	unspecified	unspecified	2007	through KfW
Nov-06	Sampo Bank	Finland	100.00	Private Sale	2007	
Oct-06	Gaz de France	France	unspecified	unspecified	July 2007	
Oct-06	LEG	Germany	100.00	unspecified	by 2008	
Sep-06	Vin & Spirit AB	Sweden	unspecified	unspecified	by 2008	
Sep-06	SAS AB	Sweden	unspecified	unspecified	unspecified	
Sep-06	OMX	Sweden	6.70	unspecified	by 2008	
Sep-06	Nordea Bank	Sweden	19.90	unspecified	by 2008	
Sep-06	TeliaSonera	Sweden	45.30	unspecified	by 2008	
Sep-06	Tote (Horserace Totaliser Board)	UK	unspecified	unspecified	unspecified	
Aug-06	Bank of Attica	Greece	38.00	unspecified	2007	
Aug-06	ATE Bank	Greece	unspecified	unspecified	2007	
Aug-06	Postal Savings Bank	Greece	15.00	Public Offer	February 2007	
Aug-06	SAS AB	Denmark	14.30	unspecified	unspecified	
Aug-06	Landesbank Berlin	Germany	80.95	unspecified	2007	
Jun-06	Alitalia	Italy	49.9	Private Sale	unspecified	
May-06	Pages Jaunes	France	up to 54	unspecified	unspecified	completed
Apr-06	DONG	Denmark	28.00	Public Offer	1H2005	postponed to 2H 2007
Mar-06	Piraeus Port Authority	Greece	unspecified	unspecified	2007	postponed
Mar-06	British Nuclear Group	UK	unspecified	Public Offer	September 2007	
Mar-06	Urenco	UK	33.00	Public Offer	unspecified	
Mar-06	Scottish Water	UK	unspecified	Public Offer	unspecified	
Feb-06	Ren	Portugal	up to 19	unspecified	end of 2006	postponed to April 2007
Feb-06	TAP Air Portugal	Portugal	unspecified	unspecified	2007	
Feb-06	ANA	Portugal	unspecified	unspecified	2007	
Feb-06	Inapa	Portugal	15.00	unspecified	2006 or 2007	
Feb-06	Portucel	Portugal	25.70	IPO	2006	completed
Feb-06	SDU NV	The Netherlands	10.90	Private Sale	2006	completed
Feb-06	OTE	Greece	20.00	unspecified	2006	June or July 2007
Feb-06	Depa	Greece	unspecified	Public Offer	unspecified	
Jan-06	Connexxion	The Netherlands	66.6	Private Sale	2006	
Jan-06	Mount Parnes Casino	Greece	51.00	IPO		
Jan-06	Dagris	France	64.70	Private Sale	2006	
Jan-06	Agricultural Bank of Greece	Greece	up to 23,8	unspecified	2006	postponed
Jan-06	Emporiki Bank	Greece	41.00	Private Sale	2006	completed
Dec-05	SEA Milan SpA	Italy	33.00	Public Offer	2006	postponed
Dec-05	Koninklijke KPN	The Netherlands	up to 8,00	Public Offer	unspecified	completed
Nov-05	Telekom Austria	Austria	up to 25,2	unspecified	after autumn 2006	
Oct-05	Scandlines AG	Denmark & Germany	100.00	Private Sale	2Q2006	
Oct-05	Eni SpA	Italy	10.00	Public Offer	2006	
Oct-05	Enel SpA	Italy	10.00	Public Offer	2006	
Oct-05	Atomic Energy Agency	UK	unspecified	Private Sale	unspecified	
Sep-05	Schiphol Airport	The Netherlands	up to 49	IPO & PS	November 2006	canceled
Sep-05	Izar's Assets	Spain	unspecified	Private Sale	unspecified	completed
Jul-05	VVF Vacances Holiday Arm	France	60.00	Private Sale	end of 2005	completed
Jun-05	GalpEnergia	Portugal	23.00	IPO	2006	completed
Feb-05	Snam Rete Gas	Italy	up to 30	unspecified	2005	postponed to 2008
Apr-05	GIMV	Belgium	30 to 35	Public Offer	unspecified	completed
Jan-05	Athens Intl. Airport	Greece	up to 55	unspecified	2005	postponed to 2007
Jan-05	Deutsche Flugsicherung	Germany	up to 75	unspecified	2005	postponed to 2007
Dec-04	Olympic Airlines	Greece	unspecified	Private Sale	2005	postponed
Oct-04	Red Electrica	Spain	10.00	Public Offer	2005	postponed to 2008
Oct-04	Iberia	Spain	5.30	Private Sale	2005	postponed to 2008
Oct-04	Endesa	Spain	3.00	Public Offer	2006	postponed to 2008
Oct-04	TV2	Denmark	51 to 66	Private Sale	1Q2005	postponed
Sep-04	RAI Radiotelevisione Italiana	Italy	20 to 30	IPO	1Q2005	canceled
Sep-04	Aguas de Portugal	Portugal	up to 49	IPO	2H2005	postponed
Sep-04	Energias de Portugal	Portugal	up to 20	Public Offer	2004	postponed to 2006 or 2007
Jun-04	Deutsche Bahn	Germany	25 to 30	IPO	2006	postponed to 2008
Jan-04	Aer Lingus	Ireland	60.00	IPO & PS	2005	completed

Source: Elaborations on *DowJones,* and *Privatization Barometer.*

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