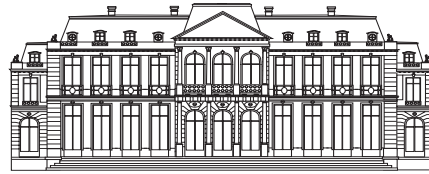


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Banks and Privatisation

The privatisation process in Italy: the role of the banks

by Rainer Masera

Rome, 18 and 19 September 1997

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**THE PRIVATISATION PROCESS IN ITALY: THE ROLE OF THE
BANKS***

by

*Rainer Masera***

1. Any privatisation process should be guided mainly by considerations of efficiency and by the need to anchor corporations and financial institutions firmly to market principles, in particular, to the objective of creating value for shareholders. As in many other countries, however, the privatisation programme in Italy was closely interwoven with the efforts to correct public finance imbalances. In fact, both processes went ahead, simultaneously. Ultimately, they mutually supported and reinforced each other.¹

The role of the banks in Italian privatisations was of major importance. Banks were active players in the process, fostering and guiding the privatisations security placements. The banks were also passive players, in that they themselves were privatised. The aim of this paper is to offer a brief account of both aspects. The time span covered is relatively short - 5 years - yet the results already achieved are of a fundamental nature.

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¹ As will be indicated, gross total proceedings of privatisations in the period 1992-1997 may total approximately 190,000 bln. lire, including Telecom, San Paolo, and Cariplo. In contrast, losses for the public sector from State owned corporations totalled some 50.000 bln. lire in the past ten years.

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In spite of many obstacles, the goals achieved have profoundly changed the landscape of the Italian economy. (Here, a tribute should be paid to the technical team at the Italian Treasury headed by its Director General, which has produced excellent results despite working under difficult conditions.)

In July 1992, the Amato Government took the first steps toward the privatisation process when it succeeded in passing urgent measures to correct the public deficit (which was close to 11,5 per cent of GDP at that time). Shortly thereafter, several State holding companies (including IRI, Enel and ENI) were transformed from public law corporations into joint stock companies, and organised under commercial law. The shares of these newly constituted companies, and of those of Banca Nazionale del Lavoro and IMI, were later transferred to the Ministry of the Treasury.

Amato, as Treasury Minister, at one time indicated that the Italian banking system was a “petrified forest”. Today that is not the case, as the pace of change in the past five years has been dramatic.

In the summer of 1992, the two major Italian investment banks – Mediobanca and IMI – were appointed as advisors to the Treasury in the formulation of the privatisation and restructuring plan for major State Holding companies (Libro Verde sulle Partecipazioni Statali). The plan set out in detail the strategy for the sale of public assets and the possible methods of privatisation: Initial Public Offering, Public Offering, Private Placement.

The plan was broadly endorsed by the Government in December of the same year. The blueprint was enacted and the time table has been broadly respected.

Some delays were incurred, notably those in the telecommunications and electricity fields, as public supervisory bodies had to be created before privatisation could proceed. This was not an easy task and the process took more time than originally anticipated.

This paper intends to focus on the relevant role of banks in the privatisation process under two main headings:

(i) The design and the implementation of bank privatisations with specific reference to Government-owned banks and banks held by Foundations.

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(ii) The “active” role of banks in the business areas of investment/ merchant banking and asset management.

An overview will then be offered of the completely new system of financial intermediaries. This new system is emerging as a result of the privatisation process and the consequent need for managers to ensure profitability and deliver value to shareholders in an open financial environment. Finally, attention will be drawn to the very strong synergies between the overall privatisation programme and the process of bank privatisation.

2. In the last five years, privatisations amounted to 60 trln. Lire (Table 1). The amount includes both direct privatisations - i.e. privatisations of companies directly owned by the Treasury Ministry - and indirect privatisations - i.e. companies owned by State holding companies. Revenues from future privatisations are estimated to amount potentially to 190 trln. Lire.²

With specific reference to privatisations of Italian banks, they first took place in early 1985 with the indirect privatisation of Mediobanca. However, it was during the last five years that most of the directly or indirectly publicly owned banks were brought to the bourse. During 1993-1994 the majority of the share capital of Credit³ and Comit was placed, through public offerings, with a limited discount, compared to their market value. In the same years, IMI's privatisation began and was completed in 1996.⁴

In the near future BNL is scheduled to be privatised. BNL, together with INA, also privatised during the same years, will contribute to define an important financial consolidation project with Banco di Napoli, whose privatisation is going to be completed in 1998.

3. The main banking groups owned by Foundations were privatised through public offering or private placement: San Paolo, Ambroveneto-CARIPLO, and

² During 1997 the Public Offering of 44.6 per cent of Telecom Italia is going to be completed.

³ See tables 6 and 7 for Credito Italiano consolidated balance sheet and profit and loss account.

⁴ See tables 10 and 11 for IMI's balance sheet and profit and loss account.

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Banca di Roma. The combined share of these three banks in terms of number of branches is about 20 per cent of the entire market (Table 1 bis). These privatisations have been realised using different models of shareholder structures, including a “stable shareholder” structure (San Paolo⁵ and Banca di Roma) and the “noyau dur” structure (Cariplo-Ambroveneto⁶).

Today, the majority of the 20 largest Italian banking groups are private. For three of these, the privatisation is going to be completed at the end of the year or at the beginning of 1998; for only a remaining few, the privatisation process is not yet scheduled.

Foundations are now playing an important role in the financial market: they represent institutional investors (such as pension funds in other countries), which can use the proceeds from their investment activity for beneficent initiatives. Unfortunately, pension funds are still missing in Italian financial markets. They are important for financial markets development. Moreover, they are vital as the population grows older and the public pension schemes become ever more unsustainable.

The lack of pension funds has implications for corporate governance as well. While a retail investor technically should be able to have his voice heard by company management, it is obvious that the representatives of large pension funds/institutional managers are able to present their views and protect their own interests much more easily. Indeed the question of protecting the rights of minority shareholders would probably be more efficaciously pursued by promoting the creation and diffusion of pension funds.

4. However, the role of the banks in the privatisation process was not only passive, but also active. This is the case of IMI, which acted as global co-ordinator in its own share placement, as well as those of INA and ENI. IMI also acted as the co-ordinator in the ILVA, Nuova Tirrena and Nuovo Pignone private placements. Moreover, Mediobanca will be one of the global co-ordinators in the Telecom Italia share placement, the largest Italian equity offering, which is going to take place at the end of the year.

⁵ See tables 8 and 9 for San Paolo’s balance sheet and profit and loss account.

⁶ See tables 2,3 and 4 for the AmbroCariplo Group’s (Pro-Forma, Merged) operating structure, the balance sheet structure, the profit structure

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5. Privatisations were particularly important in fostering the development of the Italian stock exchange, characterised, at the beginning of the privatisation process, by structural problems. On the demand side, there was a low propensity of households to invest in equities and modest presence of institutional investors. On the supply side, the number of companies listed on the Milan Stock Exchange was quite limited.

Since 1993 the Italian stock exchange market capitalisation rose from 15 per cent of GDP to the present 27 per cent and is expected to continue to climb rapidly.

The role played by banks in the privatisation process was particularly important: (i) they contributed to price information dissemination among national and foreign investors; (ii) they operated as a bridge between households savings and the Government's demand for additional capital; and (iii) they facilitated the creation of corporate controlling structures (including the "noyaux durs") which have guaranteed a stable shareholder composition.

6. Finally, banks were extremely important in the privatisation of the stock-exchange. Indeed the banks represent the vast majority of stable shareholders of Borsa Italiana S.p.A., a company created to organise and supervise Italian commodities markets. The 93/22/EEC Directive has created the possibility to increase market efficiency through the constitution of a private company, charged with the responsibility of market organisation and surveillance. This means that the typical function of market supervision and control is now considered "private", and this should be a premise for better exploiting opportunities through market participants' contributions.

7. Government privatisations, privatisation of banks controlled by Foundations, and private organisation and surveillance represent individual steps to develop and improve efficiency in the financial markets. As a result, competition should be enforced in a globalised environment and in an integrated European market. Large dimensions are still required in order to benefit from economies of scale and economies of scope.

The European financial markets offer opportunities and prospects of growth, and operational diversification for successful operators in the banking sector. Even with the premise that traditional bank intermediation is a mature sector,

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with margins that are tending to narrow, opportunities are opening up in adjoining sectors: “bancassurance”, investment banking, equity investment, securities intermediation and placement, individual and institutional financial portfolio management, asset management,⁷ risk management and capital market activity.

This requires the capacity to achieve economies of scale and scope in the production of financial services through appropriate operational and organisational strategies. Mere growth and unfocused diversification (the financial conglomerates) are unpromising paths to produce such results. Institutional de-specialisation goes hand in hand with operational specialisation: what is required, then, are multi-specialist intermediaries (financial integrated groups) with focused strategies.

Account must be taken in any event of strong pressures to establish closer ties with the financial markets, pressures that are inherent particularly in the growth of managed savings. In other words, it is a question of seizing the opportunities for complementarity, while clearly identifying the many competitive intersections and the points where operational duplication would have negative repercussions.

At the same time effectiveness cannot be achieved without costs saving and specifically, without reducing the labour cost burden, which seem to be higher in Italy, compared to the rest of Europe. This will be, in my opinion, the main aim of the banking sector, in order to compete in an open integrate market.

⁷ See tables 12, 13 and 14 for project income contribution from combined asset management activities of Credito Italiano, San Paolo and IMI.