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Comment & Analysis

CORPORATE GOVERNANCE

Hidden value: how unlisted companies are eclipsing the public equity market

The FT's new list of top enterprises in the unquoted sector reveals the striking size of operations held in state or private hands, write **Francesco Guerrera** and **Carola Hoyos**

"The publicly held corporation, the main engine of economic progress in the United States for a century, has outlived its usefulness in many sectors of the economy and is being eclipsed."

When Harvard Business School professor Michael Jensen questioned the future role of listed companies in a controversial article in 1989*, some experts greeted his predictions with thinly veiled disbelief.

One commentator professed himself "enraged" after reading Prof Jensen's "sanctimonious" analysis, while this newspaper dubbed it "extravagant".

Nearly two decades later, proponents of the primacy of publicly listed companies can no longer be so sure. In the US and Europe, a boom in takeover activity fuelled by cheap debt has seen private-equity groups buy large listed companies in sectors as diverse as hospitals and music production.

At the same time, the surge in the oil price has turned government-owned resource companies in the Middle East and Latin America into corporate behemoths. In countries like China and India, fast-growing economies and foreign investors' seemingly unquenchable desire to supply capital have offered both lumbering state monopolies and sleepy family-owned companies an unprecedented opportunity to expand their businesses and reform their governance.

With unlisted companies no longer regarded as the poor relations of their quoted counterparts, the question for investors, managers and capital markets practitioners is whether the world economy is witnessing a structural shift away from listed companies – an "eclipse" of the public corporation, as Prof Jensen put it.

"There are half a dozen ways of owning a company and there is competition between them, but what is the optimal way to own and govern corporate activity?" asks Bill Meehan, director of the Silicon Valley office of McKinsey, the management consultancy.

The Financial Times Non-Public 150, based on research by McKinsey, the consultancy, is an attempt to answer that question. As the first comprehensive catalogue of the world's largest unlisted companies, it provides a rare, and revealing, glimpse behind the veil of private and state ownership.

> Buy-out firms such as KKR, Carlyle and Blackstone have overtaken family-owned Cargill to become the largest private groups in the US

The most superficial finding of the research is one of its most striking: on some measures, unlisted companies' collective clout is comparable to that of their quoted rivals. For instance, the FT Non-Public 150 companies employ some 13m people, fewer than the 19m who work for the 150 largest listed groups but nevertheless a reminder that a substantial portion of global capitalism resides outside equity markets.

On one, crucial issue, however, private and state companies are lagging behind publicly traded companies. McKinsey estimates that the world's largest non-public 150 companies would be worth a total $7,000bn (£3,569bn, €5,313bn) if they had been listed in 2005 – roughly half the market value of their quoted counterparts (for the methodology, see www.ft.com/npc).

The yawning gap in value is a reminder that non-public ownership is not, in itself, a panacea for corporate ills and can often be used to hide poor financial and managerial performance.

The point is illustrated by a look at the top of the FT Non-Public list. Twelve of the largest 13 companies are state oil groups from developing countries. Such government-owned entities control three-quarters of the world's oil reserves and have given equity markets a wide berth for one overriding reason: the countries they serve want to maintain control over their most precious resources. Yet their role as cash cows for the all-powerful state shareholder is the source of macroeconomic and business inefficiencies that are more rarely seen among listed groups.

The crucial difference between these companies and their traded rivals is that most of their revenues go straight to the state rather than being reinvested into the business. Furthermore, on big strategic decisions, managers have to defer to political masters whose goal is not to maximise the profits of the company.

According to Nader Sultan, former chief executive of Kuwait Petroleum Corporation – which ranks fourth on the FT's list – when KPC was formed in the 1980s its revenue was about $28bn-$30bn, roughly in line with that of BP, now the world's third largest listed international energy group. "Last year, BP's total revenues were some $250bn whereas Kuwait's revenues were only $50bn-$60bn. How does one explain that? What did BP do that KPC did not do?" asks Mr Sultan, who now runs his own consultancy.

The answer is that BP grew through acquisitions and diversified into different countries and products, reinvesting its cash flow and honing its technical skills. KPC, by contrast, continued to rely on Kuwait's giant Burgan oil field with very little extra investment.

Not all national oil companies suffer from stunted growth and lack of investment. Saudi Aramco tops the Non-Public list with an estimated value of $781bn – nearly 80 per cent larger than the market capitalisation of Exxon Mobil of the US. Although the overwhelming reason for Aramco's size is that it sits on by far the world's largest conventional oil reserves, it is also one of the few national oil companies that is successfully expanding its production and revenue stream.

But in general, few experts dispute that the benefits of state ownership of natural resources, as for many other industries, are dwarfed by its drawbacks. "It is a lose/lose situation," says Prof Jensen, now a managing director at Monitor, another consultancy. "These companies destroy value in the way they run their oil fields and in the way they distribute national resources."

Experience shows that the harsh discipline required to list on equity markets can be cathartic, transforming staid monopolies into nimbler, more profitable enterprises. The Chinese government has used overseas listings as a means of foisting much-needed reforms on painfully inefficient state enterprises, including its national oil champions.

When western advisers began preparing Shanghai Petrochemical for an overseas listing in the early 1990s, for example, they were stunned to find that the state company owned a police station. The non-core asset was duly hived off before the listing.

However, Beijing has refused

to give up majority ownership of its assets, floating only a small portion of the shares in government-controlled companies – a hybrid between state and shareholder ownership. "The government wants investors' funds but it doesn't want them to gain control," says Jon Christianson, at the law firm Skadden, Arps, Slate, Meagher & Flom. "It has worked very well for China, particularly because [officials] pursued this policy regardless of equity market conditions."

The interplay between private and public markets has also been instrumental in the recent rise of buy-out funds. Helped by cheap debt and an increasingly onerous regulatory system for listed companies, as well as a focus by shareholders on short-term results, buy-out funds have lured companies away from the equity market.

Six of the top 30 companies in the FT's Non-Public list are buy-out funds that have grown exponentially over the past few years through ambitious fundraisings and takeovers of listed groups. Acquisitive firms such as Kohlberg Kravis Roberts, Carlyle Group and Blackstone Group have overtaken family-owned conglomerates like Koch and Cargill to become the largest private companies in the US.

"CEOs and boards used to look at us as renegades – and now we are regarded as the lubricants of global capitalism. We no longer have to go through the back door and as a result more and more companies have become available [to buy]," says David Rubenstein, co-founder and managing director of Carlyle.

Buy-out executives deny that their increasing reach into vital sectors of the economy is an indictment of capital markets, arguing that many of the companies they buy will eventually be relisted. But private equity's unprecedented prominence has sparked concerns of a creeping "privatisation" of large chunks of the US and European economies, which would reduce management's accountability to the wider public and deny small investors the chance to buy into these companies.

"You can't run a vibrant and innovative capital market solely on private companies," says Glenn Hubbard, a former economic adviser to US President George W. Bush and now dean of Columbia Business School. "There is a lot of value in being a public company."

Public corporations may not be facing a total eclipse but, with private equity chipping away at the influence of capital markets and many governments still jealously guarding their national treasures, the rise of non-public companies is likely to prove more than a meteoric occurrence.

**Eclipse of the Public Corporation, Harvard Business Review September-October 1989*

A WORK IN PROGRESS THAT SHEDS LIGHT ON A RICHLY DIVERSE BUSINESS LANDSCAPE

Amid the booming equity markets of the 1990s, listed companies looked poised to triumph over all others, write Bill Meehan **and** Richard Dobbs of McKinsey & Company. Family companies**, employee and state-owned corporations as well as mutuals and partnerships headed for stock markets in a stampede of initial public offerings.**

Looking across the business landscape today, however, the heterogeneity of ownership remains striking. The success of private equity has challenged the notion that the discipline imposed on managers by public markets is the path to optimal business performance. Higher energy prices have strengthened the economic position of state-owned oil companies. The growing economic importance of Asia, with its rich tradition of family business, has reinforced the role both of private companies and of quoted groups with very influential family investors.

Such diversity poses questions important to investors, managers and government ministers alike. What are the strengths and weaknesses of different forms of corporate ownership? To what extent can management practices be transferred from one to another? Under what circumstances could it make sense to change ownership structure – from, say, public to private – in pursuit of improved productivity or other advantages? In a world of competing ownership models, these questions are compelling.

The FT Non-Public 150 for the first time brings together the world's biggest unquoted companies in a single list. Based on research by McKinsey, its aim is simple: to stimulate informed debate about the impact of different ownership structures on corporate performance and health.

In compiling the list, we looked for companies that passed three main tests. First, their shares were not listed on a public stock market. Second, they were neither a joint venture nor a subsidiary of a larger entity. Third, they delivered goods or services into a commercial marketplace.

This third test explains why armies, government health systems, religious organisations and charitable foundations did not make the cut, in spite of their sometimes considerable economic muscle.

Note, however, that the FT Non-Public 150 is not a performance ranking. Judging the relative value creation of the companies on the list would require far more information than is available in the public domain for the majority of them.

For the same reason, the valuations according to which the list is ordered are not pin-point accurate. The figures represent a best guess – based solely on often incomplete public information – at the market value of these entities had the shares been listed on public markets at the end of last year.

This first iteration of the FT Non-Public 150 is without doubt a work in progress. Our hope is that the insight of Financial Times readers will enable us to refine both the list itself and our collective grasp of the strengths and weaknesses of different forms of ownership in managing corporate performance and health.

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FT Non-Public 150 - the full list

Top 150 Non-Publicly listed companies

	Company	Country	Sector	Estimated Market Value as of Dec 2005 ($bn)	Type	Type (1)
1	Saudi Aramco	Saudi Arabia	Oil gas	781	S	State owned
2	Petróleos Mexicanos (Pemex)	Mexico	Oil gas	415	S	State owned
3	Petróleos de Venezuela SA	Venezuela	Oil gas	388	S	State owned
4	Kuwait Petroleum Corporation	Kuwait	Oil gas	378	S	State owned
5	Petroliam Nasional Berhad (Petronas)	Malaysia	Oil gas	232	S	State owned
6	Sonatrach	Algeria	Oil gas	224	S	State owned
7	National Iranian Oil Company	Iran	Oil gas	220	S	State owned
8	Japan Post	Japan	Postal services	156	S	State owned
9	Pertamina	Indonesia	Oil gas	140	S	State owned
10	Nigerian National Petroleum Corporation	Nigeria	Oil gas	120	S	State owned
11	Abu Dhabi National Oil Company (ADNOC)	UAE	Oil gas	103	S	State owned
12	INOC	Iraq	Oil gas	102	S	State owned
13	Libya National Oil Company	Libya	Oil gas	99	S	State owned
14	Sparkassen-Finanzgruppe*	Germany	Banking	98	P	Association
15	State Grid Corporation of China	China	Electric utilities	87	S	State owned
16	Nippon Life Insurance Company	Japan	Insurance	87	P	Mutual
17	Kohlberg Kravis Roberts Co	United States	Private equity	83	P	Partnership
18	Qatar Petroleum	Qatar	Oil gas	78	S	State owned
19	State Farm Mutual Automobile Insurance Company	United States	Insurance	76	P	Mutual
20	European Investment Bank	Luxembourg	Banking	73	S	State owned
21	United States Postal Service	United States	Postal services	72	S	State owned
22	Carlyle Group	United States	Private equity	71	P	Partnership
23	Norinchukin Bank	Japan	Banking	66	P	Co-operative
24	Rabobank	Netherlands	Banking	62	P	Co-operative
25	Blackstone Group	United States	Private equity	60	P	Partnership
26	Texas Pacific Group	United States	Private equity	59	P	Partnership
27	Permira Advisers LLP	United Kingdom	Private equity	54	P	Partnership
28	Koch Industries	United States	Conglomerates	52	P	Family owned
29	Bain Capital, LLC	United States	Private equity	49	P	Partnership
30	Cargill, Inc.	United States	Conglomerates	48	P	Family owned
31	CVC Capital Partners Limited	United Kingdom	Private equity	46	P	Partnership
32	Apollo Advisors, LP	United States	Private equity	45	P	Partnership
33	FMR Corp	United States	Asset management	42	P	Family owned
34	Warburg Pincus LLC	United States	Private equity	42	P	Partnership
35	Boehringer Ingelheim GmbH	Germany	Pharmaceuticals	41	P	Family owned
36	Meiji Yasuda Life Insurance Company	Japan	Insurance	41	P	Mutual
37	Dai-ichi Mutual Life Insurance Company	Japan	Insurance	41	P	Mutual
38	Caja de Ahorros y Pensiones de Barcelona ("la Caixa")	Spain	Banking	37	P	Nonprofit
39	Kaiser Permanente	United States	Healthcare	36	P	Nonprofit
40	Crédit Mutuel	France	Banking	35	P	Mutual
41	The Capital Group Companies	United States	Asset management	35	P	Partnership
42	Bertelsmann AG	Germany	Media	34	P	Family owned
43	Groupe Caisse d'Epargne	France	Banking	34	P	Mutual
44	BC Partners Limited	United Kingdom	Private equity	34	P	Partnership
45	Apax Partners	United Kingdom	Private equity	33	P	Partnership
46	Egyptian General Petroleum Corporation	Egypt	Oil gas	33	S	State owned
47	China Development Bank	China	Banking	33	S	State owned
48	Cinven	United Kingdom	Private equity	32	P	Partnership
49	Japan Racing Association	Japan	Entertainment	32	S	State owned
50	Caisse des Dépôts et Consignations	France	Banking	32	S	State owned
51	Mars Inc	United States	Food & beverages	32	P	Family owned
52	Deutsche Bahn AG	Germany	Railroads	31	S	State owned
53	Silver Lake Partners	United States	Private equity	31	P	Partnership
54	Hellman Friedman Capital	United States	Private equity	31	P	Partnership
55	National Football League	United States	Entertainment	29	P	Association
56	Vanguard Group	United States	Asset management	29	P	Mutual
57	Madison Dearborn Partners	United States	Private equity	28	P	Partnership
58	Deloitte Touche Tohmatsu	United States	Professional services	27	P	Partnership
59	First Reserve Corporation	United States	Private equity	27	P	Partnership
60	Thomas H. Lee Equity Partners	United States	Private equity	27	P	Partnership
61	General Atlantic Partners	United States	Private equity	27	P	Partnership
62	China Railways	China	Railroads	25	S	State owned
63	Groupe Banque Populaire	France	Banking	25	P	Mutual
64	Trump Organization	United States	Real estate	25	P	Family owned
65	PriceWaterhouseCoopers	United States	Professional services	25	P	Other
66	Empresa Colombiana de Petróleos (Ecopetrol)	Colombia	Oil gas	24	S	State owned
67	China Southern Power Grid	China	Electric utilities	23	S	State owned
68	Loterias y Apuestas del Estado (LAE)	Spain	Entertainment	23	S	State owned
69	IKEA International A/S	Sweden	Retailers	22	P	Other
70	Corporación Nacional del Cobre de Chile (Codelco)	Chile	Metals mining	22	S	State owned
71	La Française des Jeux	France	Entertainment	22	S	State owned
72	Cox Enterprises	United States	Media	21	P	Family owned

	Company	Country	Sector	Estimated Market Value as of Dec 2005 ($bn)	Type	Type (1)
73	MassMutual Financial Group	United States	Insurance	21	P	Mutual
74	Suntory Group	Japan	Food & beverages	21	P	Family owned
75	Caja de Ahorros y Monte de Piedad de Madrid	Spain	Banking	21	P	Nonprofit
76	Ernst Young International	United States	Professional services	21	P	Partnership
77	KPMG International	Netherlands	Professional services	21	P	Co-operative
78	State Oil Company of Azerbaijan (SOCAR)	Azerbaijan	Oil gas	20	S	State owned
79	Otto GmbH Co KG	Germany	Retailers	20	P	Family owned
80	Providence Equity Partners	United States	Private equity	20	P	Partnership
81	Agricultural Bank of China	China	Banking	20	S	State owned
82	Nationwide Building Society	United Kingdom	Banking	20	P	Mutual
83	Votorantim Group	Brazil	Conglomerates	20	P	Family owned
84	Clayton, Dubilier Rice, Inc.	United States	Private equity	20	P	Partnership
85	Welsh, Carson, Anderson Stowe	United States	Private equity	20	P	Partnership
86	Vattenfall AB	Sweden	Electric utilities	19	S	State owned
87	Nationwide Mutual Insurance Company	United States	Insurance	18	P	Mutual
88	Maruhan Corporation	Japan	Entertainment	18	P	Family owned
89	Tchibo Holding AG	Germany	Food & beverages	18	P	Family owned
90	Ferrero S.p.A.	Italy	Food & beverages	18	P	Family owned
91	Comisión Federal de Electricidad	Mexico	Electric utilities	18	S	State owned
92	Landesbank Baden-Württemberg	Germany	Banking	18	S	State owned
93	JSC Russian Railways	Russia	Railroads	18	S	State owned
94	Camelot Group plc	United Kingdom	Entertainment	17	P	Other
95	USAA	United States	Insurance	17	P	Mutual
96	Citic Group	China	Conglomerates	16	S	State owned
97	Bayerische Landesbank	Germany	Banking	16	S	State owned
98	Health Care Service Corporation	United States	Healthcare	16	P	Mutual
99	Sumitomo Life Insurance Company	Japan	Insurance	16	P	Mutual
100	SC Johnson Son, Inc	United States	Consumer goods	15	P	Family owned
101	La Poste	France	Postal services	15	S	State owned
102	REWE Group	Germany	Grocery retailers	15	P	Co-operative
103	KfW Bankengruppe	Germany	Banking	14	S	State owned
104	B. Braun Melsungen AG	Germany	Healthcare	14	P	Family owned
105	De Beers Consolidated Mines Limited	South Africa	Metals mining	14	P	Family owned
106	Liberty Mutual Holding Company Inc.	United States	Insurance	13	P	Mutual
107	British Broadcasting Corp	United Kingdom	Media	13	S	State owned
108	Glencore International	Switzerland	Trading	13	P	Other
109	Edeka Group	Germany	Grocery retailers	13	P	Co-operative
110	New York State Lottery	United States	Entertainment	13	S	State owned
111	Louis Dreyfus Group	France	Conglomerates	13	P	Family owned
112	Poste Italiane SpA	Italy	Postal services	13	S	State owned
113	Société Nationale des Chemins de Fer Français	France	Railroads	13	S	State owned
114	Hydro-Québec	Canada	Electric utilities	13	S	State owned
115	Schwarz Group	Germany	Grocery retailers	13	P	Family owned
116	El Corte Inglés SA	Spain	Retailers	13	P	Family owned
117	Carlson Companies	United States	Hospitality	12	P	Family owned
118	ALDI Group	Germany	Grocery retailers	12	P	Family owned
119	Global Hyatt Corporation	United States	Hospitality	12	P	Family owned
120	Dr August Oetker KG	Germany	Food & beverages	12	P	Family owned
121	Vitol Holding BV	Netherlands	Trading	12	P	Other
122	Deutsche Zentral-Genossenschaftsbank	Germany	Banking	12	P	Co-operative
123	Nascar	United States	Entertainment	12	P	Family owned
124	Shanghai Automotive Industry Corporation	China	Automobiles parts	12	S	State owned
125	Gie Pari Mutuel Urbain	France	Entertainment	12	S	State owned
126	Auchan SA	France	Grocery retailers	12	P	Family owned
127	Northwestern Mutual Life	United States	Insurance	12	P	Mutual
128	China FAW Group Corporation	China	Automobiles parts	12	S	State owned
129	EWE AG	Germany	Electric utilities	11	S	State owned
130	Highmark Inc	United States	Healthcare	11	P	Nonprofit
131	Taiwan Power Company	Taiwan	Electric utilities	11	S	State owned
132	Tennessee Valley Authority	United States	Electric utilities	11	S	State owned
133	Dongfeng Motor Corporation	China	Automobiles parts	11	S	State owned
134	TIAA-CREF	United States	Asset management	11	P	Other
135	Independence Blue Cross	United States	Healthcare	11	P	Nonprofit
136	TC Ziraat Bankasi AS	Turkey	Banking	11	S	State owned
137	HSH Nordbank AG	Germany	Banking	11	S	State owned
138	New York Life	United States	Insurance	11	P	Mutual
139	Major League Baseball	United States	Entertainment	11	P	Association
140	Société Civile des Mousquetaires	France	Grocery retailers	11	P	Other
141	Norddeutsche Landesbank Girozentrale (Nord/LB)	Germany	Banking	10	S	State owned
142	Association des Centres Distributeurs E. Leclerc	France	Grocery retailers	10	P	Co-operative
143	National Basketball Association	United States	Entertainment	10	P	Association
144	Groupama SA	France	Insurance	9	P	Mutual
145	Würth Gruppe	Germany	Industrial supplies	9	P	Other
146	Ascension Health	United States	Healthcare	9	P	Nonprofit
147	Caixa Geral de Depósitos SA	Portugal	Banking	9	S	State owned
148	WestLB AG	Germany	Banking	9	S	Other
149	Blue Shield of California	United States	Insurance	9	P	Nonprofit
150	Indian Railways	India	Railroads	9	S	State owned

Source: McKinsey

* Sparkassen-Finanzgruppe excludes landesbanken, which are listed separately