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PUBLIC SECTOR INSTITUTIONS` FINANCIAL ASSETS

Financial assets are liquid assets that get their value from a contractual right or ownership claim. Cash, stocks, bonds, mutual funds, bank deposits – all are examples of financial assets. Unlike tangible physical assets (land, property, commodities, or other), financial assets do not necessarily have inherent physical worth or even a physical form. Rather, their value reflects factors of supply and demand in the marketplace in which they trade, as well as the degree of risk they carry [3].

Most assets are categorized as tangible, financial, or intangible. Tangible assets are physical assets that draw their value from substances or properties, such as precious metals, land, real estate, and commodities like soybeans, wheat, oil, and iron. Intangible assets are the valuable property that is not physical in nature. They include patents, trademarks, goodwill, and intellectual property.

Financial assets are in-between tangible and intangible assets. Financial assets may seem intangible – non-physical – with only the stated value on a piece of paper such as a bill or a listing on a computer screen. What that paper or listing represents, though, is a claim of ownership of an entity, like a public company, or contractual rights to payments – say, the interest income from a bond. Financial assets derive their value from a contractual claim on an underlying asset [1; 2].

This underlying asset may be either tangible or intangible. Commodities, for example, are the tangible, underlying assets that are pinned to such financial assets as commodity futures, contracts, or some exchange-traded funds. Likewise, real estate is the tangible asset associated with shares of real estate investment trusts.

According to definitions from the IAS 32 "Financial Instruments: Presentation", IAS 39 "Financial Instruments: Recognition and Measurement", IFRS 9 "Financial Instruments" financial assets include:

– cash;

– an equity instruments of an entity;

– a contractual right to receive a financial asset from another entity (receivables);

– a contractual right to exchange financial assets or liabilities with another entity under favorable conditions;

– a contract that will settle in an entity's own equity instruments.

According to the definition from IPSAS 28 "Financial instruments: presentation" a financial asset is any asset that is:

– cash;

– an equity instrument of another entity;

– a contractual right;

– a contract that will or may be settled in the entity's own equity instruments.

Businesses, as well as people, hold financial assets. In the case of an investment or asset management company, the financial assets include the money in the portfolios firm handles for clients, called assets under management. In the case of banks, financial assets include the worth of the outstanding loans it has made to customers [3].

The government of each country holds a significant and varied portfolio of financial assets. These assets include those created as a result of specific policy decisions, such as its interventions during the financial crisis and loans issued to students to encourage them into higher and further education. Financial assets also include assets held for the sole purpose of supporting the government's day-to-day cash management. The government's financial assets entitle it to receive future financial benefits and include investments such as company shares; as well as loans and cash deposits [4].

The holdings of financial assets within the public sector institutions are not novel. For many years, cash, bank deposits, and accounts receivable (money owed to an entity but not yet received) have been used to manage the flow of cash through the entity. Also, targeted funds (cash deposits and shares) have been set aside to meet future liabilities.

However, in the last couple of decades, the value and use of financial assets have increased significantly, particularly in central government. Today, financial assets are being used to fund or finance various public sector services.

For public entities, financial assets support traditional funding and delivery mechanisms. They are usually easier to buy, hold, and sell than physical assets, can be owned in small or divisible amounts, and have values that are more responsive to changing circumstances and market conditions. They can therefore introduce more liquidity and flexibility, which can be particularly important in times of change and uncertainty [1].

Financial assets can be used to discharge liabilities or provide services, while non-financial assets are normally used only for service provision, unless they are sold and thus converted back into financial assets. Financial assets and non-financial assets should be reported separately on the statement of financial position. The net financial resources/net debt and the net economic resources (accumulated surplus/deficit) measures should both be reported on the statement of financial position as they represent different perspectives of the public entities' financial position.

As the public sector's experience in using financial assets expands, the opportunities available to public entities and to the whole of government for funding and providing services will increase. Public entities use financial assets in many ways [1]:

– motivating entities or partners to act in certain ways;
– taking advantage of other ways of funding and delivering policy outcomes;
– reallocating project or program risks;
– encouraging private sector providers to take part in public projects and programs;
– promoting or influencing different investment or governance practices;
– the sale of future revenue streams for use in other projects or to increase future debt capacity;
– other uses of financial assets.

Financial assets are also being thought about and used at a whole-of-government level to provide independence in the management of assets while retaining a chosen level of control. Many local government entities hold strategic shareholdings in organizations that benefit a region's long-term prospects.

Effective financial asset management is essential to the health of the overall public finances. To get the most out of its asset holdings, the government must manage them effectively and professionally and be aware of the risks that influence the income streams that drive their value.

References

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