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Importance of Keeping a Government Share in Pakistani Companies after Privatization

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This study investigates the operational and financial performances of private and semi- government companies in Pakistan. Our sample consisted of 80 private and 12 semi government companies for which we used the word "government companies" or SOEs or "public companies". With computer aid we calculated different Profitability Ratios, Activity Ratios, Long Term Solvency Position Ratios and Liquidity Ratios for both types of companies during the period of 1999 – 2006. Results of analysis showed that public owned companies have achieved better performance than private companies in terms of profitability, long term solvency position and liquidity. However no significant differences were found between private and public companies in respect of turnover ratios.

1. Introduction

It is generally believed that there will be performance difference between government and private ownership because of the monitoring devices associated with private ownership. It is assumed that publicly owned enterprises will perform more poorly than private sector firms. The reason may be that politicians want managers of government firms to employ excess labor, and appointments are made on basis of political reasons rather than merit. Also government companies have to forgo maximum profits for social welfare purposes. So we may expect government companies to be less efficient than private companies. The prevailing concept that the private sector is better than the Government sector is stronger in developed countries. But, in case of developing countries like Pakistan, private sectors are also suffering from the causes which prevail in the public sector. Corruption, lack of competitive pressure, lack of basic infrastructure etc. are some problems which may reduce efficiency of the private companies. In developing countries, the private sector is shy, inexperienced, and unequipped to embrace on rapid industrialization. Moreover, in our case, Government organizations are not completely owned by the government, and shares of varying levels of ownerships are held by the general public. So it does make sense to compare the performance of both types even in terms of profitability.

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1.1 Objectives of study

The objective of this study is to determine whether privatized companies are performing better than mixed companies/state owned companies or mixed enterprises are better than privatized.

1.2 Focus of the Study

In Pakistan, the financial data is not maintained by any authority. Therefore, it was not possible to collect data for all companies we included initially in our sample. We are focusing only to the Islamabad Stock Exchange because the sample will give us a better script. The firms were selected using convenience sampling as the data was collected for all the firms which were available in Islamabad stock exchange. There are 243 companies listed on Islamabad Exchange. The government has shareholdings in almost 16 companies ranging from 26% to 90%. There are about 227 private companies in which Government share holding is zero percent. This thesis covers the manufacturing and merchandising sectors of Islamabad Stock Exchange which include major sectors like Textile, cement, sugar, power, generality oil & Gas, glass and ceramics, paper & board, food and personal core products.

1.3 Data set

Data used in this study was acquired with the help of computers from Islamabad Stock Exchange (ISE), internet and websites of different companies. The period covered by the study extends to eight years starting from 1999 through 2006. We have selected a sample of 92 companies (80 Private and 12 State-owned), listed on Islamabad stock exchange, including firms from different sectors of our economy, and managed to obtain their disclosed financial statements.

1.4 Variables:

All the variables stated below have bee used to test the hypothesis of our study.

1.4.1 Dependent variable

Performance is the dependent variable which is affected by other explanatory variables

1.4.2 Explanatory variables:

1.4.2.1 Profitability Ratios:

1. Gross Profit Ratio GPR
2. Operating Ratio OR
3. Operating Profit Ratio OPR
4. Net Profit Ratio NPR
5. Return on Investments ROI
6. Return on Capital Employed ROCE
7. Return on Equity Capital ROEC
8. Earning Per Share EPS

1.4.2.2 Activity Ratios:

1. Inventory Turnover Ratio ITR

2. Debtor Turnover Ratio DTR
3. Fixed Assets Turnover Ratio FATR
4. Total Assets Turnover Ratio TOTR
5. Capital Employed Turnover Ratio CETR

1.4.2.3 Long-Term Solvency Ratios:

1. Debt-Equity Ratio DER
2. Equity Ratio ER
3. Fixed Assets to Net-worth FA-NW
4. Interest Coverage Ratio ICR

1.4.2.4 Liquidity Ratios:

1. Current Ratio CR
2. Liquid Ratio LR
3. Average collection period ACP

2: Descriptive analysis

For further analysis, different Profitability Ratios, Activity Ratios, Long term Solvency Position Ratios and Liquidity Ratios have been shown graphically for eight years i.e. from 1999 to 2006. For comparative purpose, ratios of private sector as well as government sector have been used side by side in the same figure in order to make different ion between performances of both types of organizations, to make the graph, the data is arranged on yearly basis and average of each year is used to show trend.

2.1 The Profitability Ratios:

Table 2.1

Srl #	Ratios	Sector	1999	2000	2001	2002	2003	2004	2005	2006
1	Gross Profit Ratio%	Government-Owned	17.48	13.78	12.63	18.36	19.07	23.00	22.82	21.57
		Private	16.88	18.16	15.21	17.18	15.00	15.36	16.43	15.82
2	Operating Ratio%	Government-Owned	96.79	98.35	92.80	90.49	89.81	85.32	84.14	84.45
		Private	98.95	101.33	89.92	88.46	91.26	90.82	87.62	87.92
3	Operating Profit Ratio%	Government-Owned	3.21	1.65	7.20	9.51	10.19	14.68	15.86	15.55
		Private	1.05	-1.33	10.08	11.54	8.74	9.18	12.38	12.08
4	Net Profit Ratio%	Government-Owned	4.43	0.12	1.85	4.04	6.69	11.58	12.15	11.78
		Private	3.08	-0.42	7.56	6.72	5.66	8.36	8.51	7.27
5	Return on Investment	Government-Owned	0.11	0.00	0.08	0.09	0.18	0.24	0.24	0.26
		Private	0.05	-0.01	0.18	0.15	0.13	0.19	0.17	0.15
6	Return on Capital Employed%	Government-Owned	5.45	0.19	3.68	6.92	11.12	15.77	13.22	18.39
		Private	2.97	-0.48	10.89	9.13	8.42	13.47	11.16	9.59
7	Return on Equity Capital	Government-Owned	0.17	0.01	0.10	0.17	0.28	0.41	0.42	0.51
		Private	0.10	-0.02	0.42	0.35	0.33	0.54	0.46	0.52
8	Earning Per Share (EPS)	Government-Owned	1.72	0.06	0.96	1.69	2.77	4.11	4.20	5.13
		Private	1.03	-0.16	4.24	3.53	3.27	5.45	4.58	5.18

The Above Table shows trends in different profitability ratios for government and private companies for the years 1999 to 2006. Government companies have shown better performance than Private companies in terms of Gross Profit Ratio, Operating Ratio, Operating Profit Ratio, Net Profit Ratio, Return on Investment and Return on Capital

Employed over the period under review. For the same period performance with respect to Return on Equity Capital is almost same for both types of companies. EPS for private companies has been slightly better than of their government counterparts for the periods from 1999 to 2006. As a whole, companies partly owned by government have performed better than the private companies during the period under review.

2.2 The Activity Ratios:

Table 2.2

Srl #	Ratios	Sector	1999	2000	2001	2002	2003	2004	2005	2006
1	Inventory Turnover Ratio	Government Owned	2.38	2.90	3.31	1.82	2.08	2.05	11.70	10.71
		Private	2.00	2.25	2.60	2.41	2.68	2.74	2.94	5.00
2	Debtor Turnover Ratio	Government Owned	5.45	6.21	7.04	7.12	7.13	8.41	7.67	7.27
		Private	7.28	9.00	9.65	9.97	12.76	13.53	6.22	5.61
3	Fixed Assets Turnover Ratio	Government Owned	1.25	1.45	1.78	1.87	1.99	1.92	0.97	1.27
		Private	1.05	1.16	1.60	1.57	1.68	1.86	1.36	1.51
4	Total Assets Turnover Ratio	Government Owned	0.77	0.88	1.02	0.73	0.74	0.66	0.61	0.72
		Private	0.67	0.75	0.91	0.89	0.93	0.96	0.79	0.86
5	Capital Employed Turnover Ratio	Government Owned	1.23	1.56	1.99	1.71	1.66	1.36	1.09	1.56
		Private	0.97	1.14	1.44	1.36	1.49	1.61	1.31	1.32

It is evident from the above Table that for government companies Inventory Turnover Ratio and Debtor Turnover Ratio have been better than private companies during the period from 1999 to 2006. Private companies have been slightly better than government companies with respect to Fixed Assets T/O and Total Assets T/O Ratios. As a whole, the result is mixed as far as Activity Ratios for both types of companies are concerned.

2.3 Long Term Solvency Ratios:

Table 2.3

Srl #	Ratios	Sector	1999	2000	2001	2002	2003	2004	2005	2006
1	Debt Equity Ratio	Government-Owned	2.34	2.56	3.05	2.09	2.52	2.17	2.24	2.10
		Private	1.64	1.67	1.62	1.49	1.42	1.34	1.50	1.36
2	Equity Ratio	Government-Owned	0.3	0.281	0.247	0.321	0.281	0.314	0.311	0.325
		Private	0.379	0.375	0.382	0.401	0.413	0.428	0.395	0.431
3	Fixed Assets to Net Worth	Government-Owned	2.056	2.16	2.323	1.219	1.32	1.092	2.04	1.743
		Private	1.693	1.726	1.488	1.406	1.338	1.206	1.469	1.326
4	Interest Coverage	Government-Owned			2.288	3.043	7.221	18.14	22.52	31.24
		Private			2.419	2.302	2.759	4.947	5.192	4.163

The above table shows that both types of companies have reduced their reliance on external financing over the period. For government companies Debt Equity Ratio decreased from 2.34 in 1999 to 2.10 in 2006 with net decrease of 10.25% and for private companies it decrease from 1.64 in 1999 to 1.36 in 2006, thus showing a decrease of 17% in Debt Equity Ratio. Equity Ratio shows proportion of Shareholder's Fund in Total Assets of the company. The above table shows that for government companies Equity Ratio increased form 0.30 to 0.32 and for private companies it increase from 0.38 to 0.43 for the period 1999-2006. It is also evident from the above table that for both government and private companies, the Ratio of Fixed Assets to Net-worth has decreased over the period. For government companies it decreased from 2.06 to 1.74 with a decrease of 15.53% and for private companies it decreased from 1.69 to 1.33 with net decrease of 21.3% for the same period. The above table shows

that there is a huge difference of Interest Coverage Ratio between government and private companies. Interest Coverage Ratio for government companies increased from 2.29 to 31.24, showing remarkable increase of 1196% to cover the interest payment ability of the company and for private companies there is an increase of only 72% in the ratio from 2.42 to 4.16 for the period.

2.4 Liquidity Ratios:

Table 2.4

Srl #	Ratios	Sector	1999	2000	2001	2002	2003	2004	2005	2006
1	Current Ratio	Government-Owned	0.94	0.82	0.78	0.77	0.76	0.81	0.82	0.79
		Private	1.18	1.03	1.17	1.25	1.21	1.19	1.15	1.13
2	Liquidity Ratio	Government-Owned	0.233	0.22	0.223	0.188	0.233	0.333	0.725	0.697
		Private	0.261	0.231	0.286	0.366	0.415	0.387	0.722	0.702
3	Average Collection Period	Government-Owned	66.08	57.97	51.14	50.57	50.47	42.8	46.94	49.52
		Private	49.44	39.99	37.3	36.1	28.2	26.62	57.85	64.2

Current Ratio for both private and government companies have not been satisfactory for the years 1999 to 2006. The above table describes bad performance of both types of companies in this respect. Current Ratio for government companies decreased from 0.94 to 0.79, and for private companies it decreased from 1.18 to 1.13. The above figure shows that Current Ratio for both private government companies has been almost equal over the period of eight years. For government companies Current Ratio increased from 0.23 in 1999 to 0.70 in 2006 and for private companies it increased from 0.26 in 1999 to 0.70 in 2006. The Average Collection Period of government companies has decreased from 66.08 days in 1999 to 49.52 days in 2006 and for private companies it increased from 49.44 days in 1999 to 64.20 days in 2006. The reduction in collection period for government companies shows efficiency of public sector in its debt collection and as compared with private companies which have been inefficient for receivables collection.

Section 3: Quantitative Analysis

For quantitative analysis we used *t*-test for important profitability, inventory turnover, and long term solvency position and liquidity ratios of the government and private companies. The results of t-tests are presented below.

3.1 *t*-test for Gross Profit Ratio:

Table 3.1

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	29.56
	Pvt.	14.28
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	2.476	
P-Value*	0.015	

* Significant at 5% level

The above table shows *t*-test of the gross profit ratio for government and private owned companies; *P-value* is also significant. The table shows that there is difference in gross profit ratio of government and private companies. So, there is difference of performance in private and government companies.

3.2 *t*-test for Operating Ratio

Table 3.2

***t*-Test: Two-Sample Assuming Equal Variances**		
Mean	Govt.	62.64
	Pvt.	90.32
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	(3.154)	
P-Value*	0.002	

***** Significant at 5% level

In the above table, both *t*-criterion and *p*-value are significant. It means that there is a difference in Operating Ratio of government companies and private companies.

3.3 *t*-test for Net Profit Ratio:

Table 3.3

***t*-Test: Two-Sample Assuming Equal Variances**		
Mean	Govt.	19.02
	Pvt.	2.89
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	3.050	
P-Value*	0.003	

***** Significant at 5% level

The table above shows that both *t*-criterion and *p*-value are significant. This result shows difference in the net profit ratios of both sectors.

3.4 *t*-test for Inventory Turnover Ratio:

In above table result of *t*-test of inventory turnover ratios for both types of companies is shown. The *P-value* is significant at 10% level. Although we cannot reject our null hypothesis at 5% level, at 10% level of significance we may accept alternative H_1;

Table 3.4

***t*-Test: Two-Sample Assuming Equal Variances**		
Mean	Govt.	16.69
	Pvt.	7.77
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	1.887	
P-Value*	0.062	

***** Significant at 10% level

and reject the hypothesis that both sectors perform at same level. Thus, at 10% level of significance we find a difference in inventory turnover ratio in both sectors.

3.5 *t*-test for Debtor Turnover Ratio:

Table 3.5

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	3.71
	Pvt.	8.02
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	(1.867)	
P-Value*	0.065	

***** Significant at 10% level

In the above table *t*-test is applied for Debtor Turnover Ratio of government and private companies in Pakistan. The *P-value* is not significant at 5% level. But at 10% level of significance we may reject our null hypothesis and accept alternative one.

3.6 *t*-test for Total Assets Turnover Ratio:

Table 3.6

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	0.81
	Pvt.	1.01
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static	0.802	
P-Value	0.425	

From the above table, we cannot reject the null hypothesis, and conclude that there is no significant difference between total asset turnover ratios in both sectors' companies.

3.7 *t*-test for Capital Employed Turnover Ratio:

Table 3.7

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	2.25
	Pvt.	1.57
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static	0.407	
P-Value	0.685	

The Critical *t*-test and *p*-value shown above indicate that there is no significant difference between both sectors in terms of the capital employed turnover ratio.

3.8 *t*-test for Debt Equity Ratio:

Table 3.8

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	2.18
	Pvt.	0.45
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static	1.950*	
P-Value	0.054 *	

***** Significant at 10% level

In the above table t-test for debt Equity ratio for companies of both sectors is shown. Critical value of t-statistic and *p*-value are not significant at 5% level but are at the 10%. The ratios are border-line to the 5% level which encourage us to accept that there is a difference at 5% level if we apply a one-tail test.

3.9 *t*-test for Interest Coverage Ratio:

Table 3.9

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	774.09
	Pvt.	(36.19)
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	3.208	
P-Value*	0.002	

***** Significant at 5% level

In the above table, both *t*-statistic and *p*- value are significant at 5% level. Thus, we may reject our null hypothesis and accept the alternative, and conclude that interest coverage ratio for companies partly owned by the government are different from private companies in Pakistan.

3.10 *t*-test for Current Ratio:

Table 3.10

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	3.48
	Pvt.	1.47
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	2.472	
P-Value*	0.015	

***** Significant at 5% level

In the above table for the current ratio, both *t*-statistic and *p*- value are significant at 5% level. Thus, we may reject our null hypothesis and accept alternate hypothesis and conclude that the Current ratio for companies partly owned by the government is different from that of totally private companies in Pakistan.

3.11 *t*-test for Liquid Ratio:

Table 3.11

t-Test: Two-Sample Assuming Equal Variances		
Mean	Govt.	2.36
	Pvt.	0.48
Observations	Govt.	12
	Pvt.	80
t-Critical	1.987	
t-Static*	3.183	
P-Value*	0.002	

***** Significant at 5% level

In the above table, the result of *t*-test for Liquidity ratios of both types of companies is shown. Both *t*-statistic and *p*- value are significant at 5% level. Thus, we may reject our null hypothesis and accept the alternate one, and conclude that the Liquid ratio for companies partly owned by the government is different from that of the private companies in Pakistan.

4. Conclusion:

Comparative performance of partly state owned and fully private companies has been a topic of discussion since 1980s, when a wave of state owned organizations began to blow over many countries of the world. In most of the researches it was concluded that private companies outperformed government companies or that performance of state owned companies improved after privatization. In Pakistan, after establishment of the Privatization Commission of Pakistan in 1991, many state owned companies were privatized and the process is still underway. In our descriptive as well as quantitative analysis it was revealed that performance of companies that still have the government as co-owner in terms of profitability and liquidity and long term solvency position has been better than fully private companies over the period 1999 – 2006. But, no significant differences in terms of turnover ratios of the government sector and private sector were found. However, companies that are still partly owned by the government have improved their liquidity position over the period. To conclude, we can say that performance of state partly-owned companies have been better than the fully privatized companies. Results may be surprising because the general assumption is that private companies have better performance than government companies. It was our intention to compare those government companies included in the study sample with those fully private or fully privatized for the purpose of our analysis. It is suggested therefore that government should sell part of its ownership in companies to the private concerns but should not privatize them in full, and must retain its influence over the companies.

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