# GROWTH PROFIT MARGIN PERFORMANCE OF PRIVATIZED SOEs: A MEAN COMPARISON APPROACH

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## ABSTRACT

*Privatization as a reform policy package has been adopted by both developed and developing countries' economies. Nigeria as a developing country has large public enterprises. These enterprises performed below expectation due to multiple problems. Technical committee was set up to privatize these enterprises. The paper used secondary data sourced from the companies' financial reports. The data has been analyzed by using mean comparison technique. The gross profit margin (GPM) model 45 percent out of the sampled privatized SOEs had their mean difference increased after privatization and six companies had their mean difference increase above the average.*

## 1. INTRODUCTION:

Privatization of government enterprises is one of the key reforms strategies for developed and developing the economies. Several countries and transition economies have embarked on privatization programme as a means for fostering economic growth and attaining macroeconomic stability, reducing public sector borrowing and subvention to state owned enterprises (SOEs) (White and Bhatia, 1998). The spate of empirical work on privatization had increased, albeit with a microeconomic orientation that emphasizes efficiency gains Jerome (2008),La Porta and López-de-Silanes (1997); D'Souza and Megginson (1999); Boubakri and Cosset (1998); Dewenter and Malatesta (2001). Yet despite the upsurge in research, our empirical knowledge of the post privatization performance enterprises in Africa and particularly in Nigeria is limited. Aside the theoretical predictions, not much is known about the performance of privatized companies.

Nigeria as a developing country witnessed the growing involvement of state in economic activities. The expansion of state owned enterprises (SOEs) into diverse economic activities was viewed as an important strategy for fostering rapid economic growth and development. Nigeria's public enterprise sector is one of the largest in sub-Saharan Africa in terms of scale and scope as reflected in the absolute numbers of enterprises. These covered industries (manufacturing, agriculture, services, public utilities and infrastructure). They also includes: telecommunications,

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power, steel, petrochemicals, fertilizer, vehicle assembly, banks, insurance and hotels etc, Jerome, (2008). Shares of employment, value added and gross fixed capital formation of public enterprises generally exceeded those of other African countries. The estimated 1,500 enterprises accounted for about 57% of aggregate fixed capital investment and about 66% of formal sector employment by 1997.

## 2. NIGERIAN PUBLIC ENTERPRISES PERFORMANCE

In the opinion of Jerome, (2008) the persistence failure of Nigeria's public enterprises has been extraordinary. He further argued that the enterprises consumed massive subsidies but deliver intermittent services. Therefore the returns of the large investments on the SOEs have generally been poor, and sometimes negative. It has been estimated that total investment in the public enterprise sector exceeded US$35 billion, comprising US$12.5 billion in equity, US$10.2 billion in government loans. These investments yield US$1.5 billion in dividends and loan repayments Federal Government of Nigeria, (FGN, 1986). Net outflows from the government to the public enterprise sector have been estimated at US$2 billion annually (Callaghy and Wilson, 1988).

Many studies and reports such as by Jerome (2008), El-Rufai (2001) and TCPC (1993) documented the reasons for the poor performance of public enterprises Nigeria. This includes presence of multiple objectives and internal inefficiencies. Also in most often political consideration rather than economic viability govern the location of industries. Inefficiencies to misuse of monopoly powers, especially in infrastructure, resulted in unreliable delivery and availability of services. Other contributory factor is the lack of regulatory frameworks that impede competition, discourage private investment. There is also weak capacity to implement reform; and gross mismanagement Jerome, (2008). This made Nigeria under-achieved its growth potential as a result of public enterprise sector weighed down by inefficiency and massive corruption.

Corruption accordant World Bank, (1995) has been a major source of fiscal problems and a drag on growth to Nigeria. In the wake of the economic recession, the activities of public enterprises attracted more attention and underwent closer scrutiny, much of it centering on their poor performance and the burden impose on government finance. The poor financial returns from these enterprises, against the background of severe macroeconomic imbalance and public sector crisis, precipitated the concern of government towards privatization. The privatization programme was subsequently adopted as part of the structural adjustment programme in this country.

The programme is expected to:
• Restructure and rationalize the public sector in order to lessen the preponderance of unproductive investments;

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• Reorient the enterprises towards performance improvement and overall efficiency;

• Ensure positive returns on investments in commercialized public enterprises;

• Check absolute dependence of commercially-oriented parastatals on the treasury and encourage their patronage of the capital market.

## 3. METHODOLOGY

This paper used secondary data because focuses on the performance of privatize enterprises it therefore requires two set of data pre- and post-privatization data. A total of 35 companies are selected. The research sourced the financial data of the privatized SOEs for the period of 10 years. The data collection is limited to those SOEs that are fully privatized to private investors through public offer of shares because only SOEs that are privatized in this way generate post financial and accounting data that is directly comparable to pre-privatization data. The data on the performance of privatized firms are calculated covering five years before and five years after privatization. Thereafter mean value of each variable is calculated. Year of privatization is excluded from the mean calculation since it is phase of both state and private ownership. The data are sourced from the annual reports of the privatized enterprises.

Mean comparison method of analysis is used to analyze the data collected. The mean comparison measures differences between population or samples. In the mean comparison method, independent and dependent sample (matched sample) can be chosen. Since this study is related to measuring firm performance pre- and post- privatization, using the dependent sample is the most appropriate one. Specifically, according to Corder and Dele (2009), the mean comparison method is used for comparing the firm performance for pre-privatization ($B$) and post-privatization ($A$) periods. Let say $X_B$ and $X_A$ are measurement firm performance for pre-privatization and post-privatization periods of sampled group of firm, respectively. The means of firm performance of each sampled group for pre-privatization and post-privatization periods are represented by $\bar{X}_B$ and $\bar{X}_A$, respectively. A higher mean in the succeeding era suggests improvement in the performance of the sampled groups. Throughout the mean comparison analysis, it is assumed that dependent random samples are selected from one population, the population of differences, $D = X_B - X_A$ is continuous, and the $n$ differences are a random sample from the population of differences.

In the opinion of Corder and Dele (2009), two dependent samples mean is used to determine if the difference between the sampled groups is statistically significant. For examining the differences mean performance of grouped firms for pre- and post- privatization periods, $H_0$: $\mu_B - \mu_A = 0$ against $H_1 : \mu_B - \mu_A \neq 0$ are used. The $t$ – test is used to test the hypotheses. In common with other statistical test, the two sample $t$ – test requires that the data have an

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approximately normal distribution and the standard deviations from the two samples are approximately equal.

## 4. THE RESULTS

GPM indicates the amount of profit from the sale of goods produced. In the opinion of Kihn (1993), it shows profit relative to sales after production cost, also it indicates relationship between production and selling price. A higher *GPM* is a sign of good management and indicate the company is doing well. The results of the previous studies such as Baily (1986), Magginson *et al.* (1994), Boubakari and Cosset (1998) and D'Souza and Magginson (1999), privatization leads to higher *GPM*. This research use *GPM* to measure the effect of privatization on the performance of privatized SOEs. Therefore, based on previous research findings, privatization has positive effects on the performance of the growth profit margin of privatized SOEs. The empirical results of average mean of *GPM* before and after privatization revealed that only 11 privatized SOEs from the total sampled had their mean average increased after privatization. Nine of these companies recorded average values mean after privatization above the overall average.

Table 1 presents the empirical results of average mean of *GPM* before and after privatization.

Table 6.3:      Mean Comparison Results of Gross Profit Margin

| Subsector | Name of Firm | Mean | | Mean |
|---|---|---|---|---|
| | | Before | After | Difference |
| Oil | Conoil | 0.08 | 0.04 | -0.05 |
| | Forte Oil | 0.56 | 0.07 | -0.50 |
| | MRS | 0.02 | 0.02 | 0.00 |
| | Mobil Oil | 0.07 | 0.07 | 0.00 |
| | Okomu Oil | 0.50 | 0.24 | -0.26 |
| | Oando Oil | 0.52 | 1.08 | 0.56 |
| | Total Oil | 0.08 | 0.76 | 0.68 |
| Manufacturing | Naitonal Salt Company | 0.79 | 0.71 | -0.08 |
| | Ashaka Cement | 0.42 | 0.18 | -0.24 |
| | Benue Cement | 0.77 | 0.32 | -0.45 |
| | CCNN Plc | 0.08 | 0.11 | 0.02 |
| | WAP Nig Plc | 1.00 | 0.27 | -0.74 |
| Insurance | AIICO Plc | 0.33 | 1.08 | 0.75 |
| | Continental Reinsurance | 0.20 | 0.15 | -0.05 |
| | Conterstone Plc | 0.17 | 0.13 | -0.03 |
| | Cosolidate Insurance | 0.15 | 0.12 | -0.02 |
| | Crusader Nig. Plc | 1.00 | 1.13 | 0.13 |

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| | | | | |
|---|---|---|---|---|
| | Int. Energy Insurance | 0.20 | 0.25 | 0.05 |
| | Equity Insurance | 0.12 | 0.13 | 0.01 |
| | Guinea Insurance | 0.33 | 0.25 | -0.09 |
| | Lasaco Assuarance | 1.09 | 0.23 | -0.85 |
| | Law Union Insurance | 0.23 | 0.08 | -0.15 |
| | Linkage Insurance | 0.13 | 0.12 | -0.02 |
| | Niger Insurance | 0.22 | 0.22 | 0.00 |
| | Oasis Insurance | 0.34 | 0.47 | 0.13 |
| | Prestige Insurance | 0.17 | 0.26 | 0.09 |
| | Regency Insurance | 0.10 | 0.11 | 0.01 |
| | Royal Exchange Insurance | 0.46 | 0.61 | 0.15 |
| | Standard Insurance | 0.93 | 1.29 | 0.36 |
| | Unic Insurance | 0.44 | 0.43 | -0.01 |
| | Unity Insurance | 0.12 | 0.20 | 0.08 |
| | Universal Insurance | 3.17 | 0.83 | -2.34 |
| Banking | First Bank Plc | 0.35 | 0.23 | -0.12 |
| | UBA Plc | 0.24 | 0.20 | -0.05 |
| | Union Bank Plc | 0.72 | 0.31 | -0.41 |
| | Overall Average | 0.46 | 0.36 | -0.10 |

Plc is public liability company.

The result of the sampled SOEs in the oil marketing sector showed that, five companies had their mean difference increased after privatization. Total Oil Company recorded the highest performance. This company had 0.08 mean before privatization, it improved to 0.76 after privatizing the company. The 0.68 mean difference recorded by the company is above the average.

These results suggested that the proportion of oil marketing companies whose GPM mean improve after privatization are more than those that did not experience mean improvement after privatization. The result of this study is opposite to the findings of Huang and Song (2002) on financial and operating performance of China's newly listed H-firms. They recorded a steady decrease of return on sales after the companies were listed.

In manufacturing subsector, Only CCNN plc recorded positive mean difference. The company has 0.08 mean before privatization, the mean increased to 0.11 after privatization. The sector show a very weak mean difference results after privatization. This may not unconnected to the withdrawal of subsidies and other benefits by government as a results of privatization. The weak mean difference improvement, although is not expected but is in line with the finding of Hakro and Akram (2009). The result of their study revealed that cement and chemical fertilizer companies experienced negative mean change after privatization.

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The insurance service subsector has the highest number of sampled privatized SOEs. Half of the companies in the sector recorded mean difference increase after privatization and the performances of five are above the average. AIICO insurance company plc recorded the highest GPM mean change. It had 0.33 mean before privatization, the figure improved to 1.08 after privatization. The mean difference performance of the company is above the average. The standard insurance company plc is next to AIICO in term of mean difference improvement. The company has 0.93 mean before privatization, the mean increased to 1.29 after privatization. Therefore, the 0.36 mean difference recorded is above the calculated average. The results of the insurance companies are in line with the findings of Boubakri and Cosset (1999) study. They reported mean improvement in their sampled SOEs.

In the banking sector, all the three sampled banks recorded negative mean difference. First Bank had highest negative mean difference of -0.12, the bank has a mean of 0.35 before privatization, and it dropped down to 0.23 after privatization. The negative mean difference of the bank is statistically significant at 10 percent. From the result, it can be deduced that privatization did not improved mean of the banks. The unfavorable GPM results in the banking subsector may not be unconnected to the removal of government accounts and the steep competition in the sector. D'souza and Megginson (1999) adduced these factors as the reason for the negative results in their study.

In the GPM model, there is a negative mean difference across the sectors and companies after privatization. The aggregate negative mean difference represents 54 percent and is not statistically significant except First Bank. In the final analysis of the GPM model, 46 percent of the companies demonstrated increased of mean difference after privatization.

It is noticed that there is differences in term of performance improvement among the sectors. The sectors that recorded deterioted improvement include manufacturing, oil marketing and banks. Most the SOEs in these sectors enjoyed higher protection and more subventions from the government, they were not so exposed to the discipline of the capital market. So the level of exposure to the dictate of capital market and the degree of government protection is a possible reason for the performance differences among the sectors. The insurance sector which is less protected by government performed better than the rest of the sectors.

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