

121

Short-Term Impact of Privatization on Firm Performance in Ethiopia

(The case of Leather Industry)

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Abstract

Short-term Impact of Privatization on Firm Performance in Ethiopia: The case of Leather Industry

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Privatization is a very recent experience in Ethiopia though it is a worldwide phenomenon in the past three decades. This study aimed at investigating the potential impact of privatization on the financial and operating performance of State Owned Enterprises (SOEs) in the Leather sub sector as an effort to find out how the privatization of public enterprises may affect the financial and operational performance of these enterprises. The data were obtained from the annual financial reports of seven firms in the stated industry four years before and four years after privatization. Performance criteria were calculated and compared to determine whether there are differences among them in the pre- and post-privatization periods. The findings revealed that while privatization did not seriously affect privatized enterprises operating performance and profitability, it led to liquidity improvement, debt reduction, increased investments, and a decline in overstaffing.

Key words: Privatization and Efficiency

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Table of Contents

List of Tables

List of Acronyms

CHAPTER ONE

1. Introduction

1.1. Background of the study	1
1.2. Statement of the problem	5
1.3. Research questions	6
1.4. Objective of the study	6
1.5. Significance of the study	7
1.6. Limitations of the study	7
1.7. Scope of the study	8
1.8. Organization of the study	8

CHAPTER TWO

2. Literature Review

2.1 Over view of Privatization	9
2.2 The Theoretical review	10
2.3 A Survey of the Empirical Literature	15
2.4 Privatization and Efficiency	19
2.5 Extent and Methods of Privatization	21
2.6 Selection of firms to be privatized	23

2.7 Privatization Process in Ethiopia.....	24
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CHAPTER THREE

3. Methodology	
3.1.Research design	30
3.2.Study subjects	30
3.3.Sampling size and Sampling methods	31
3.4.Method of data collection	31
3.5.Data analysis	32

CHAPTER FOUR

4. Findings and Discussions	
4.1.Enterprise Performance	36
4.2.Empirical Results	40
4.3.Result Discussion	52

CHAPTER FIVE

5. Summary, Conclusions and Recommendations	
5.1. Summary and conclusions	59
5.2. Recommendations	61

- References
- Appendices

List of Table

Table 1: The Results of Profitability Ratios before and after Privatization.....	41
Table 1.1 Company wise analysis by profitability	42
Table 2: The Results of Operating Performance Ratios before and after Privatization	44
Table 2.1 Company wise analysis by operating efficiency.....	45
Table 3: The Results of Liquidity Ratios before and after Privatization	47
Table 4: The Results of Leverage Ratios before and after Privatization	48
Table 5: The Results of capital expenditure Ratios before and after Privatization	49
Table 6: The Results of employment data before and after Privatization	50
Table 7 - Post privatization actual performance Vs Expected results	51

Acronyms

AAU	Addis Ababa University
AT	Asset Turnover
D/A	Debt-Asset Ratio
D/E	Debt- Equity Ratio
EBIT	Earnings before Interest and Tax
EMPL	Employment
EPA	Ethiopian Privatization Agency
EPS	Earning per share
GOE	Government of Ethiopia
INEFF	Income Efficiency
PPESA	Privatization and Public Enterprises Supervising Agency
ROA	Return on Asset
ROE	Return on Equity
ROI	Return on Investment
ROS	Return on Sales
SALEFF	Sales Efficiency
S.C	Share Company
SOEs	State Owned Enterprises
UK	United Kingdom

CHAPTER ONE

Introduction

1.1. Background of the study

Privatization is the act of reducing the role of government, or increasing the role of private sector, in an activity or in the ownership of assets. Privatization has been prescribed as a means of improving the efficiency and profitability of public enterprises, which are not performing well. The privatization of government owned enterprises is nowadays a large-scale process for the transfer of state owned enterprises to the private sector (Mohammed, 2004).

Privatization, as an instrument for development is finding significant currency in industrial and developing countries throughout the world and is one of the important components of socio-economic reform programmes being implemented around the world. The major aim of this policy is to reduce the drain on the government resources, caused by the persistent losses of public enterprises, and to create greater opportunities for private investors to expand and modernize these enterprises with the aim of liberalizing the economic environment for rapid industrialization (Nellis, 1999).

As quoted from Getachew (2003), privatization is a policy prescription where governments are compelled to or willingly take action to reduce their role to regulate and direct the behavior of private actors in the economy. Deregulation is aimed to remove restrictions and barriers of the economy by making them less important. The interest for

privatization is entrenched in the belief that the private sector is more efficient than the public sector or state owned enterprises in producing and delivering goods and services. Moreover, the entry of new private enterprises could introduce competition where public sector enjoyed monopoly. A shift from a policy of reserving certain economic activities once owned and done by the public sector implies a reduction in the relative position of the state. By so doing the public enterprises would be forced to go commercial and respond to the market discipline (Fekru, 2000).

Since the beginning of the 1980s, the world has undergone a major shift in thinking about the appropriate economic role of the state. Privatization of State Owned Enterprises (SOEs) has been at the core of this change ever since. Britain and France initiated privatization planning (Galini et al, 2004). In developed and developing countries more than one hundred governments have privatized at least some of their SOEs”.

Jerome (2002) argues that “following the apparently successful privatization program in Britain-privatization gained a considerable momentum in developing countries given its endorsement by the multilateral financial institution as a major plan of adjustment policy and reinforced by the need to reduced government expenditure in the face of burgeoning fiscal deficits”.

The privatization has become an important phenomenon in both developed and developing countries. Over the past decade, privatization attempts have been occurring at an increasing rate, especially in developing countries. The compound annual average growth rate was around 10 % between 1990 and 2000, with global privatization revenues jumping from \$ 25 billion in 1990 to \$ 200 billion in 2000. The number of countries that

have implemented privatization policies has exceeded 110, not to mention that privatization has touched almost every aspect of economic activity (Shahdeh, K.S. 2002).

Primary reason governments attempt to privatize SOEs is to improve the efficiency of these SOEs and, thus, to reduce the budgetary burden on the state. Other reasons for privatization attempts include raising revenues, creating popular capitalism, rewarding political loyalists, placating external financing agencies, decreasing the administrative burden of state bureaucracy, and making the private sector responsible for needed enterprise investments (Nellis, 1999).

The efficiency of the social and economic infrastructure has been generally recognized as a critical factor in the development of an economy. Although there are a number of theoretical and empirical studies on privatization, they are still far from any definitive conclusion. Limi, (2003) argues that the empirical work indicates a mixed picture; the privatization may or may not have a positive effect on firm performance.

The advocates of privatization, such as Jackson and M. Price (1990) argued that great performance improvements would result from the change of enterprise ownership which redefines the enterprise objectives and manager incentives. The performance of privatized enterprises will be judged in terms of profits and return on capital. On the other hand the opponents of privatization tend to argue that simply changing ownership is not sufficient, and indeed may not even be necessary to improve firm performance. Increased competition and organizational reforms have been more important than the change of ownership.

After the formulation of the new economic policy by the government in the 1990s, the country is striding forward and registering tangible results in the sphere of economic development which is expected to benefit the people in a meaningful way. In order to realize the above stated objective, the government is working hard to enable the private sector so that it would become the engine of the industrial development strategy. The government, in line with its commitment to encourage the private sector, has started a privatization programme (PPESA News, 2011).

The Ethiopian privatization agency (EPA) was established in February of 1994 by proclamations No. 87/1994 and 146/1998. Since then, EPA has become the lead agency in carrying out the process of privatization of public enterprise with the objectives of

- Generating revenue required for financing development activities undertaken by the government
- Changing the role and participation of the government in the economy to enable it to exert more effort on activities requiring its attention; and
- Promoting the country's economic development through encouraging the expansion of the private sector.

According to PPESA News (2011) so far 287 public enterprises have been privatized and transferred to domestic and foreign investors. In the leather sub sector, nine enterprises have changed hands from the public to private sectors since the leather industry has been one of the major traditional industries together with the coffee and garment industries, but it is now at a turning point to change itself from a traditional industry to a modern

industry to penetrate the international high value-added leather market, under the strong initiative of the GOE.

Therefore, this paper has been conducted to analyze the impact of privatization on firm performance in the leather sub sector is important since there are high expectation placed upon privatization, by policy makers and the public at large, to improve enterprise performance.

1.2. Statement of the problem

In its acceptance of privatization policies, Ethiopia has relied on a number of assumptions about the merits of privatization. These assumptions are supported by the experience of the countries which had preceded Ethiopia in privatizing SOEs. The most prominent of these assumptions is that private ownership leads to the improvement of efficiency of companies.

In their survey article, Ehrlich et al (1994) suggests that private ownership leads to higher rates of productivity growth and declining costs in the long run. Similarly the advocates of privatization tend to argue that private ownership is more efficient than public one. Their arguments are based on the claims that the change in enterprise's ownership redefines the enterprise objectives and the manager's incentive to reduce cost and increase profit (Shirely and Nellis, 1991).

Although Ethiopia's first privatization attempts started in 1994, the literature on privatization in Ethiopia lacks empirical research which aims at scientifically and objectively assessing this experience to examine the degree of success of these

privatization attempts in terms of the realization of their desired outcomes. Thus, the purpose of the present study is to empirically investigate the effect of privatization on the financial and operational performance of selected SOEs in Ethiopia.

1.3. Research questions

More specifically, the study attempts to answer the following two questions:

- Does privatization improve the financial and operational performance of privatized Leather companies in Ethiopia?
- Is privatization conducive to the improvement of the Ethiopian privatized Leather companies' performance efficiency indicators such as profitability, operative efficiency, investment expenditure, and financial elevation?

1.4. Objective of the study

1.4.1. General objective of the study

The general objective of this study is to evaluate the impact of privatization on the financial and operational performance of privatized enterprises. To achieve this objective, the study addresses the theoretical aspects by reviewing concepts, methods, impact, and experience of some developing and developed countries.

1.4.2. Specific objectives of the study

The paper has the following specific objectives.

- To see the impact of privatization on the profitability of SOEs

- To assess the effects of privatization on SOEs operating efficiency
- To see the impact of privatization on SOEs capital structure
- To examine the impact of privatization on SOEs leverage and capital investment spending.
- To observe the impact of privatization on SOEs employment.

1.5. Significance of the study

Since 1998 Ethiopia embarked upon privatization although relatively young compared to other developing nations. So far, many enterprises have been privatized but the reason behind privatization in the country is based on the experience of other countries positive result over privatization. In view of this fact this study informs policy makers and the public in large about the real picture of the Ethiopian Privatization by assessing the effect of privatization on the financial performance of SOEs. The study also makes the concerned bodies alert about privatization. Furthermore, other interested researchers might take this study as a base for detailed and further studies.

1.6. Limitations of the study

The project had financial sponsor but it was not enough. As a result, it was found difficult to extend the study over to other sectors other than in the leather sub-sector and even within the leather sub-sector it was un able to collect information primarily from the factories within the industry, which would have given a better overview of the impact of privatization on firm performance. Besides time has been a universal constraint.

Another major constraint was poor documentation in the concerned bodies' particularly in the Ethiopian Privatization Agency and also empirical literatures were not available in the country on this specific subject for essay reference.

1.7. Scope of the study

This study is concentrated only to the analysis of the effect of privatization on firm performance of SOE in Ethiopia. For the reasons indicated in the limitation of the study section, privileges provided to the industry sector and more specifically it examines the impact of privatization on the financial performance of firms in the Leather sub sector.

The data set for this study obtains from Ethiopian firms that had been privatized in the Leather sub sector and had at least 4 years of both pre- and post- privatization data.

1.8. Organization of the study

The remainder of this paper is organized as follows; chapter two presents the overview of privatization, the theoretical and empirical review of literature, and depicts the process of privatization in Ethiopia. Chapter three provides the methodology and describes the data used, followed by chapter four that deals with the empirical findings from the investigation made through analysis of the effects of privatization on enterprise performance as measured in terms of firm profitability, productivity, leverage and liquidity. Finally, in chapter five a summary of findings and some conclusions and recommendations are offered.

CHAPTER TWO

Literature Review

2.1 Over view of Privatization

There is a wide range of theoretical and empirical literature relating to the impact of privatization on financial performance of privatized enterprises. Shirley (2000) argues that two decades of experience have not settled the debate over how much ownership matters about positive influence on financial performance of privatized enterprises.

The relative performances of public and private enterprises have been documented by Boardman and Nining (1989) who indicate that “in the world outside the united states private enterprise outperform both SOEs and mixed enterprise in competitive environment”.

The advocates of privatization tend to argue that private ownership is more efficient than public one. Their arguments are based on the claims that the change in enterprise’s ownership redefines the enterprise objectives and the manager’s incentive to reduce cost and increase profit (Shirely and Nellis, 1991).

In contrast, another group considers that SOEs are superior to the private ones. They argued that SOEs could be efficient in net financial position if their control system is suitable and they have clear goals and objectives. Along the same line Claessens and Djankov (1998) still claim that SOEs perform better than private enterprises. This implies that private sector ownership is no guarantee of good performance. In this respect it is

noted that private sector firms, in every corner of the world, go bankrupt every day; and that there are, in fact, examples of SOEs, such as those in United State, Germany, Brazil, and South Korea, that perform quite well.

Third view finds no difference between the performances of both types of enterprises (Martin, 1993). He argues that any attempt to evaluate the performance of the SOEs must take into account the multiplicity of objectives (economic, social and political) that it must pursue as compared to simple profitability objective that is the characteristic of most private enterprises.

2.2 The Theoretical review

Is public or private ownership more likely to be efficient? This question has induced a fair amount of debate in the literature on privatization. Specifically, the literature in this issue can be divided into two branches: the social view and the agency view.¹ The social view is in favor of public ownership while the agency view supports private ownership. The theoretical arguments supporting these views are briefly summarized as follows:

A. The social view

The social view argues that public ownership has several advantages over private ownership.

¹ See Truong D. Loc, Nguyen H. Dang, and Nguyen V. Ngan (2007), Equalization and Firm Performance: The Case of Vietnam, Final Report of an EADN individual research grant project, Cantho.

Traditionally, state-owned enterprises are viewed as instruments capable of curing market failures by implementing pricing policies that take social marginal costs and benefits of production into account (Shapiro and Willig, 1990).

Additionally, state-owned enterprises are controlled by governments, maximizing social welfare and improving decisions of private firms when monopoly power or externalities lead to a divergence between private and social objectives (Shleifer and Vishny, 1994). For example, under non-competitive conditions, efficiency requires a single company to exist, but with the maximizing profit objective, the private company will exploit monopoly power to charge too high of a price and produce too low of a quantity. This potential inefficiency can be solved by public ownership.

B. The agency view

Under perfect competition, more recent economic literature has taken a much less flattering view of public ownership and a more favorable view of private ownership. This literature stresses that principal reasons for privatization are the existence of information asymmetries and incomplete contracting problems, leading to severe incentive problems and therefore serious inefficiency of state-owned enterprises (agency view). Within the agency view, there are two complementary strands of the literature depending on whether the critical agency conflict is with the manager or with the politician. The first, termed the managerial view, argues that SOE managers may lack high-powered incentives or proper monitoring. The second, termed the political view, stresses that political interference in the firm results in excessive employment, poor choices of product and

location, lack of investments, and ill-defined incentives for managers (Shapiro and Willig, 1990; Shleifer and Nishny, 1994).

1. The managerial view

According to the managerial view, poor monitoring and lack of high-powered incentives result in inefficiency of state-owned enterprises. Managers (agents) in both private and state owned firms are assumed to maximize their own utility, rather than of the organization or its owners (principals). In private companies, this divergence is reduced through both external mechanisms, such as markets for managers, capital market, and corporate control, and internal mechanisms, such as managerial participation in ownership, reward systems, and the board of directors. However, these mechanisms are virtually absent in state-owned companies in Truong D. Loc, et al (2007).

Moreover, the owner-managers relationship is broken down into two other agency relationships, the public as owners to politicians and politicians to managers, which effectively reduce the incentive for monitoring managers' behavior. The privatization and monitoring incentives are essentially discussed in Vickers and Yarrow (1991). Specifically, they argue that privatization leads the manager to focus on profit goals because under private ownership, the management is directly supervised by shareholders, although it might be constrained in its actions by a legal system. However, under public ownership, the management is monitored by the government, which in turn can be view as an agent of the voting population. In addition, based on the assumption that shareholders expect the firm to maximize profits, Yarrow (1986) notes that managerial incentives depend on the separation of ownership and control, the availability of

performance information to shareholders, the effectiveness of the takeover mechanism and legal constraints.

Moreover, Vickers and Yarrow (1991) analyze a specific trade-off between a public company and a private regulated one. The authors argue that benefits of private ownership stem from the assumption that shareholders will not expropriate investments of manager in the company's assets while the government could re-deploy the investments to serve social goals. Thus, the manager's investment incentives are better under private ownership. However, the cost of private ownership, according to this study, is that the company's manager has to report to two different parties: the regulators and the shareholders. Therefore, conflicts between the regulators' and the shareholders' objectives would create an incentive problem to induce inefficiency of the company.

2. The political view

The political view argues that poor performance of state-owned enterprises is caused by distortions in both the objective function that managers seek to maximize and the constraints they face, the so-called soft budget constraint. Specifically, managers of SOEs pursue strategies, such as excess employment, that satisfy the political objectives of politician who control them (Boycko et al., 1996). Moreover, politicians impose objectives on these firms that would help them to gain votes, but might conflict with efficiency. The reason why managers are able to do this without facing the threat of bankruptcy relates to the second distortion, the soft budget constraint.

As cited in Truong D. Loc, et al (2007), in any situation in which the firms have been engaged in unwise investments, it will be in the interest of the central government to bail the firm out using the public budget. The rationale for this relies on the fact that the bankruptcy of companies would have a high political cost, whose burden would be distributed within a well-defined political group, like unions. On the other hand, the cost of the bailout can be spread over the taxpayers, a less organized and larger group in society, with diversified interests and preferences. Therefore, the threat of bankruptcy is no credible under public ownership (Sheshinski and López-calva, 2003).

Shapiro and Willig (1990) argue that the government is better informed about the firm under nationalization than under privatization. The reason is that ownership of the firm gives privileged access to its accounting system. From a welfare-maximizing point of view, if the government is less informed, it is more difficult for the government to pursue its private agenda. Hence, privatization is seen as a constraint on the “malevolent” government.

Further, Boycko et al. (1996) develop a model of privatization to explain the relative inefficiency of state-owned companies and their performance improvements after privatization. The assumption of their model is that performance of SOEs is poor because these companies pursue the objectives of politicians, such as excess employment levels, rather than maximize efficiency. Indeed, the politicians prefer high employment level because it helps them to gain votes. In addition, the manager of the SOE in this model is assumed to represent for private shareholders.

By allowing for corruption, the manager can bribe politicians for lower employment, and in some cases corruption can improve efficiency. However, a corruption contract is not usually legal and enforceable, so inefficiency of SOEs is not necessarily cured in this way. In the private company, the manager will set the employment at the efficient level because the company's objective is to maximize profit. In this case, politicians can use government subsidies to convince the manager to keep up employment level. It is likely that providing new subsidies for high employment level is politically more costly to the politicians than using foregone profit for this purpose because the flow of subsidies is more easily observable than foregone profit of a firm (Truong D. Loc et al, 2007).

2.3 A Survey of the Empirical Literature

With the increase in privatizations by governments over the last decades, the empirical literature concerning privatization has also grown. Most empirical studies related to privatization focus on examining the effect of privatization on firm performance. This section reviews the main empirical evidence on the impact of privatization on firm performance.

A. Positive Impact of Privatization on Firm Performance.

Baboukri and Cosset (1998) analyzed the financial performance of 79 newly privatized enterprises in 21 developing countries between 1980 and 1992 and found significant increase in profitability, operating efficiency, capital investment, employment and decline in leverage. The change in profitability and efficiency were large in middle- income countries than in low-income ones.

Meggison et al. (1994) in a large scale and more comprehensive research compared the pre and post- privatization performance of 61 enterprises in 18 countries, out of which 12 were from developed countries and 6 from developing ones, in 32 industries that experienced full or partial privatization through public share offerings during the period 1961-1990. The result of this research indicate that most enterprises experienced increase in profitability, efficiency, capital investment spending, employment and dividends payment, while they witnessed a significant decrease in leverage.

In developing countries, most of the findings on assessment of financial performance before and after privatization concluded that privatization improves the performance of the enterprise (Kikri and Nellis, 2004).

In the same vein Pinheiro (1996) studied the impact of privatization on financial performance in Brazil. The research analyzed the financial performance of 50 privatized enterprises before and after privatization, using data during 1990 to 1994. The result of the research confirmed that privatization brings a significant improvement on the financial performance of the privatized enterprises.

As quoted from Mohammed (2004) at the case study level, Eckel, and Singhal (1997) analyze the effects of privatization on the performance of British Airways and argue that when a firm is privatized several factors change simultaneously such as ownership and a firm's objectives. These factors, among others, ultimately improve the economic efficiency of the firm. Ramamurti (1997) also finds a significant improvement in labor productivity of Argentine national freight following privatization although that improvement was accompanied by a significant decrease in employment.

Ehrlich et al. (1994) use a sample of twenty-three comparable international airlines of different ownership categories over the period 1973-83. Their results suggest that private ownership leads to higher rates of productivity growth and declining costs in the long run, and that these differences are not affected by the regulatory environment.

Earle and Telegdy (2002) find that privatization increases labor productivity growth in their heterogeneous sample of Romanian firms. Frydman et al. (1999), find that privatization to outsider owners has significant effects on revenue performance, but not on cost reduction using data from the Czech Republic, Hungary and Poland, of 218 state owned firms, of which 128 were privatized during the period from 1990 to 1994.²

As cited in Cagla Okten et al. (2005), in the study of 233 privatized Mexican firms, find that ratios of investment to sales and investment to fixed assets significantly increase after privatization while employment significantly decreases (La Porta and Lopez-De-Silanes, 1999).

Warzynski (2003) in his study of 300 Ukrainian firms finds that competition does not have a significant effect on firm performance measured by productivity and profitability while privatization has a marginal positive significant effect on profitability and an insignificant effect on productivity.³

² See Cagla Okten and et al; [2005]: the Effects of Privatization on Efficiency: How Does Privatization Work, Bilkent University, Department of Economics, Ankara, Turkey

³ See Cagla Okten and et al; [2005]: the Effects of Privatization on Efficiency: How Does Privatization Work, Bilkent University, Department of Economics, Ankara, Turkey.

B. Negative impact of privatization on firm performance

Another line of thinking indicates the possibility that performance improvements could be realized without a change of ownership. Havrylyshyn and McGehegion (2001) indicate that the overall impact of privatization – in spite of expectations – is not always positive. There are many empirical studies about the impact of different types of privatization on enterprise performance.

Wallsten (2000) undertook a research of privatized enterprise in telecom sector in Africa and Latin America and found that competition was associated with network improvements, while privatization by itself did not yield financial performance change.

Harper (2001) documents different findings for 178 Czech firms that were included in the first wave of voucher privatization. He concludes that profitability and efficiency decreased immediately following privatization.

Villalonga (2000) examines twenty-four Spanish firms from different industries and finds that privatization does not increase firm efficiency (defined as rate of return on assets. He argues that political factors such as the business cycle during which the firm is privatized and foreign ownership are important determinants of firm efficiency).

As cited in Cagla Okten and et al. (2005) finds that in the telecommunications sector, privatization by itself does not appear to generate many benefits and is negatively correlated with main line penetration. He points out the importance of regulatory framework ensuing from privatization as he finds that privatization combined with the

existence of a separate regulator is correlated with increased connection capacity and labor efficiency as measured by employees per main line.

C. Mixed impact of privatization on firm performance

As far as studies on individual countries are concerned, Martin and Parker (1995) find mixed results in performance -in terms of profitability and efficiency- for 11 privatized firms in the UK.

As quoted in Cagla Okten and et al. (2005) some recent studies control for unobserved firm heterogeneity using firm fixed effects in a panel data analysis (Earle and Telegdy, 2002; Ehrlich et al., 1994; Frydman et al., 1999; Villalonga, 2000; Wallsten, 2001). The results of these studies on privatization and firm performance are mixed.

From the above discussion of international experience it is evident that the impact of privatization on financial performance is mixed. While some studies indicate that privatization could lead to an improvement in profitability, efficiency, outputs, capital investment spending and debt ratio (i.e. positive impacts), there are studies which show the contrary (negative impacts). Yet some other studies found that no difference in financial performance between privatized enterprises and those enterprises still owned by the state (neutral impacts).

2.4. Privatization and Efficiency

Historically SOEs were established to ensure political control of production, better provision of public goods, more effective ways of dealing with externalities, leading of

economic development in the absence of “well functioning” markets, and guaranteeing full employment and equitable income distribution. The economic performance of many SOEs proved disappointing, however, and since the early 1980s privatization started to be advocated as a means of establishing clear property rights, providing economic incentives and stimulating superior economic performance of firms and economies at large (see Bernardo et al, 2004). One argument for privatization is that firms under central planning are inefficiently large and their divestitures, combined with privatization, constitute a desirable way to improve corporate performance (see Hanousek, et al, 2008). Another argument for privatization stresses the fact that the objectives imposed by the state as owner in SOEs are not necessarily consistent with profit maximization (see Saul et al 1991).

Even if the state as owner seeks to maximize the profits of its firms, problems of corporate governance may still lead to inferior performance. Outside owners whether private or state do not have full information about corporate performance, so firm specific rents may be appropriated by the managers. However, private ownership may place more effective constraints on managers’ discretionary behavior, via high-powered incentives for managers or through the operation of the market for corporate control, though if ownership is dispersed, owners may face a free rider problem in which the individual returns to monitoring by each owner are less than the costs (Shleifer and Vishny, 1994).

Moreover, Roman et al. (2000) have argued that the imposition of hard budget constraints on SOEs will not induce strategic restructuring because entrepreneurial incentives associated with outside investor will still be absent. This relates to the incomplete

contracts ideas of Hart et al (1988) that have been used to argue that state managers tend to make routine decisions whereas private owners would engage in non-routine decisions and stimulate entrepreneurship. In the presence of external shocks, privatized firms are hence thought to move more readily into new markets and product lines and hence be less likely to lay off workers than SOEs. This suggests that privatization might only be effective when control shifts to new owners, who are thereby able to change the managers.

Perhaps the main warning to the efficiency arguments in support of private ownership concerns the welfare dilemmas when private firms provide public goods and/or have natural monopoly power (Jean-Jacques et al, 1993). If firms have monopoly power, privatization can be harmful even if productive efficiency of a firm increases, unless there are adequate regulatory controls or sufficiently rapid entry. Monopoly power also creates a dilemma for the state as owner in a privatization process; firms that are privatized with monopoly power can be sold for higher prices than if the company is broken up to create a more competitive market structure. Similarly, if corporate governance provisions for private firms are negligent, company assets may be stolen and misallocated. Monopoly power may hence explain a deviation between empirical results concerning profitability and sales.

2.5. Extent and Methods of Privatization

The fact that the state owned almost every industrial firm raised questions about how much privatization should be undertaken, by what methods and at what rate. In practice, most countries decided to privatize a large number of firms rather quickly (Estrin, 1994)

and were therefore forced to innovate in privatization methods in order to address the unprecedented issues of scale and the political urgency for speed.

Some authors have suggested that deficiencies in some of these the new methods of privatization, notably the widespread use of forms of “mass” privatization, whereby shares are distributed at nominal prices to the population at large, may explain the apparent initial deficiencies in the impact of the policy (Stiglitz et al, 2002).The arguments for fast privatization were that (a) price liberalization and other reforms would not provide sufficient incentives for SOEs to restructure and become competitive, (b) state would not be able to resist intervening in SOEs and (c) managers (and/or workers) would de capitalize firms in the absence of rapid clarification of property rights. In contrast, Roland et al. (1994) argued that gradual privatization was needed because the political backlash to rapid privatization of all firms would be unacceptable. Argument for gradualism was that it allowed the government to pursue a strategy that necessitated fewer workers being immediately laid off and that it would reduce uncertainty.

Mass privatization led to ownership structures that were initially highly dispersed because the entire adult population of the country, or all insiders to each firm, was allocated vouchers with which to purchase the shares of the company. Mass privatization was also argued to hinder the establishment of effective corporate governance, especially when long "agency chains" were created by the emergence of financial intermediaries holding privatization vouchers (Stiglitz, 2002).

2.6. Selection of firms to be privatized

Whatever the privatization methods used, it is likely that firms are not assigned for privatization at random. This has important implications for econometric work assessing the impact of privatization on company performance because it implies that studies that treat the allocation of firms for privatization as random or do not adequately control for the non-random selection may potentially overstate the positive effect of privatization on performance. Realizing this shortcoming, Gupta et al. (2008) analyzes the problem that arises in the studies that ignore the fact that better or worse firms may be privatized first. They note that there may be several reasons why a government may choose to sequence the privatization of SOEs. First, the government may incur excessively high transaction and congestion costs if it tries to privatize all firms simultaneously. Second, by sequencing it may reveal information about the firms to investors (later buyers may observe the quality of the firms sold earlier) if there is uncertainty about the quality of the firms being privatized, or avoid political opposition to reforms (Roland, 1994).

Gupta et al. (2008) consider five competing government objectives for privatization: i) maximizing Pareto efficiency through resource allocation; ii) maximizing public goodwill from the free transfers of shares to the public; iii) minimizing political costs stemming from unemployment; iv) maximizing efficiency through information gains and v) maximizing privatization revenues. They use firm-level data from the Czech Republic to test the competing theoretical predictions about the sequencing of privatization and find strong evidence that the firms that the government privatized first were more profitable, were firms in downstream industries, and in industries subject to greater

demand uncertainty. Privatizing more profitable firms first is hence inconsistent with maximizing Pareto efficiency but it is consistent with the model of maximizing privatization revenues, maximizing public goodwill and minimizing the political cost of unemployment. However, the implication of the political cost model that employment growth in the firm's industry should affect sequencing is not supported by the results.

2.7. Privatization Process in Ethiopia

Privatization is a very recent phenomenon in Ethiopia. It was initiated in 1994 through the establishment of the Ethiopian Privatization Agency by proclamation N0.87/ 1994. In 1998, further amendment was made through proclamation N0.146/1998 that allowed the Agency to have more mandate and responsibility, among other things, to exercise post privatization monitoring activities.

A. Privatization Objectives and Strategies

At the start of the program, the privatization objective was not clearly defined nor has the government made the privatization motive crystal clear, except that it was generally considered as part of the prevailing economic reform that covers a broad spectrum of economic deregulation. However, according to the Ethiopian Privatization Agency (EPA, 1998), the government has lately come up with some objectives and made them public. These include:

- Maximizing revenue and ensure a better ownership – the private sector
- Relieving tied resources and re-deploy into other areas of higher priority.

- Create a dynamic and new industrial entrepreneur group that will be a capably and partner in development
- Attract new investors into areas of strategic importance in the national economic development, by providing an easy access to already develop and operating businesses.

Thus, the primary aim of the program is to generate revenue required for financing development programmes undertaken by the government. At the same time it was seen as a necessary initiative to enable state enterprises to compete and survive in the new economic environment through change in ownership. The change in ownership is perceived to be a necessary condition to subject state owned enterprises to market discipline and to ensure that they raise their standards of performance. At the same time, it was also aimed to redefine the role and participation of the government in the economic sector and allow it focus to only those areas it can perform well and do things that necessarily require its involvement. Privatization being a globally prescribed phenomenon - endorsed under structural adjustment program; its objectives are not significantly different among countries.

In order to realize its objective, the privatization program in Ethiopia has defined strategies and values with the aim to ensure maximum revenue, competitive bidding system and transparency. To facilitate the privatization, reforms have also been taken in regard to involving the private sector in areas of business, which were earlier reserved only for the public sector. Creating favorable conditions for private investment has been considered as a reinforcement mechanism to give rise to competitive environment. That

is why promoting economic development through expanding the private sector is underscored as one of the prime objectives of privatization (EPA, 1998).

B. Privatization Modalities

As cited in Getachew (2003) as is the case for many African countries, the selection of privatization modalities by and large depends on the nature of the country's economy and the size and nature of the enterprises. The main privatization modality used by the Ethiopian Privatization Agency is asset sale method through competitive bidding. Accordingly, the majority of small retail trade outlets, small hotels, restaurants, manufacturing and mining enterprises are privatized via auction through competitive tender method. Although asset sale through competitive tender is the principal method, employee and Management Buy Outs (retail outlets, hotels, and restaurants through safety net program), and restitutions to former owners represent a significant proportion of transactions.

However, in order to promote a more complex privatization process of medium and large-scale enterprises, a creation of wider opportunity for the involvement of domestic and foreign investors through the use of alternative modalities were imperative. Consequently a wide range of privatization methods and modalities such as share sales by competitive tender, Restricted Tender and Negotiated Sale, Lease and sale, management contract and joint venture methods etc have been introduced.

C. Process of Privatization

Steps in the process of privatization by and large depend on the types of strategies used and arrangements made taking into account values and objectives to be met, such as transparency, credibility, speeding up of privatization and so on. There is no uniform approach or standard form of procedures employed across the board among countries.

According to the Ethiopian Privatization Agency (EPA, 2002), the main arm of the Agency responsible for the privatization process is the Privatization Operation Division, which has four departments and one services department. The major task of the division is to undertake the preparation of enterprises for privatization (pre privatization process), privatizing enterprises (implementation) and monitoring post privatization, which includes assessing the impact of privatization on the economy (post privatization). In the courses of carrying out these tasks, the privatization process involves the following activities:

- Due Diligence
- Valuation and Auditing
- Transforming the public Enterprises in to share Company
- Preparing Information memoranda
- The Bidding Process
- Transfer of enterprise

The first step of the process pertains to report production that diligently identify and address problems and constraints related to the privatization of an enterprise. The second step involves Valuation and Auditing. Ideally the market should set the price of the

public enterprises. However, for many practical reasons, this is not feasible, and actual asset evaluation is necessary-often used as auction base price. Fixed asset valuation of buildings, processing plant and machinery vehicles and equipments etc., is done to reflect market-based prices. In connection with this, a financial audit activity is also done to clearly indicate the financial positions of the enterprise-very vital information for potential buyers. This step also includes financial restructuring and business evaluation processes. Debt rescheduling, different forms of write-off and measures that ensure the viability of the proposed share company are activities in the restructuring process. Business valuation on the other hand takes into account the performance of the enterprise over time, financial strength, market conditions etc., in addition to asset and liabilities of the enterprise. The third step pertains to actual transfer of the enterprise in to a new share company. As we shall see later, one of the benefits of transferring the enterprise into Share Company is to allow domestic investors to have access to involve in the privatization process by pooling their resources together, which otherwise is difficult to finance big purchases individually (EPA, 2002).

The fourth step involves the preparation of information memorandum document which provide ample information to prospective buyers with regard to company performance, product and outputs market, customers, sales outlets, suppliers, human resource, competitors, etc., and the country's economic profile in general. The fifth step is the bidding process, which includes preparation of bid documents, advertising and selling bids, bid evaluation, negotiation and signing of contract agreements. The final step of the privatization process is the legal transfer of the enterprise from government to the private

sector. This may involve the handing over process of the enterprise to the buyer, share transfer etc, depending on the mode of transfer (EPA, 2002).

As one could see from the above discussion, the process of privatization involves a number of steps that require activities to be carried out meticulously. This is because issues such as credibility, transparency, and etc, very vital for the success of the privatization, are concerns to be dealt in each step of the process. The credibility of the privatization process is vital to its success. In order to ensure credibility, all matters pertaining to privatization should be done with clarity and certainty. This involves granting the rule of law, adequate publicity, and make sure that each activity in each step is carried out as stipulated in the privatization policy, statements, announcements, legislations, and proclamations regarding the privatization process. Transparency facilitates the success of the privatization. It is thus, important to ensure a maximum transparency for public support privatization. To make certain the smooth operation of the privatization process, it is therefore, vital that each activity in each step should be viewed and valued in reference to the degree of transparency ensured (EPA, 2002).

CHAPTER THREE

Research Methodology

3.1 Research design

As noted earlier the main purpose of this paper is to examine the impact of privatization on the financial performance of SOEs. The research design used in the paper is a “before-and-after” design (also known as the pre-test/post- test design). A “before and after” design can be described as two sets of cross section observations on the same population to ascertain the nature of the change in the phenomenon or variable (s), between two points of time. The change is measured by comparing the difference in the phenomenon or variables at the before and after periods [see, for example, Leary, (1991)].

To measure the effects of privatization on firm performance, we first calculate performance measures for every firm for the years before and after privatization. Then, the mean of each measure is computed for each firm over the pre-privatization (years -4 to -1) and post-privatization (years +1 to +4) periods.

3.2 Study subjects

Research participants are those SOEs which had been privatized in Leather sub sector. From this sector, seven enterprises were included in the study. Namely, Universal Leather Articles Factory, Awash Tannery Factory, Ethiopian Pickling & Tanning Factory, Addis Ababa Tannery S.C, Modjo Tannery S.C, Tikur Abay Shoe S.C, and

Ethiopia Tannery S.C. The study subject is to know the impact of privatization on the financial performance of SOEs in Ethiopia.

3.3 Sampling size and Sampling methods

The data set for this study obtained from Ethiopian firms that had been privatized in Leather sub sector and had at least 4 years of both pre- and post- privatization data. In fact there are nine factories within the industry among them seven of them met the data requirement and taken all of them as a sample for this study.

3.4 Method of data collection data analysis

The purpose of this study is to evaluate the impact of privatization on the financial and operational performance of the SOEs in Ethiopia. The study used different financial and operating performance criteria and ratios of SOEs in the pre-privatization and post-privatization eras. These criteria include profitability, operating performance, liquidity, leverage, employment and investment expenditure.

The main data used are data sheets, while the sources are: 7 selected privatized enterprises, The Ethiopian Privatization Agency and other relevant institutions. Information on privatization gathered from reports and other documents used as secondary sources. The main data set contains the annual financial statements (balance sheets, income statements and cash flows), audited reports of the privatized enterprises. These include secondary data sources and informal interview of relevant people in the sector.

3.5 Data analysis

In order to analyze the performance of SOEs, the year of privatization is assigned a zero value and the average ratio of the company's performance is calculated. It is calculated and compared to determine whether there are differences among them in the pre-and post-privatization periods.

Description of Variables

Profitability:

This is measured by several proxies including return on sales (usually denoted by ROS), return on assets (ROA) and return on equity (ROE) ratios. (ROS) refers to earnings before interest and tax (denoted by EBIT) divided by sales, while (ROA) refers to EBIT divided by assets; and (ROE) refers to EBIT by equity.

Return on sales (ROS)

It measures the amount of profit generated on sales.

$$\text{ROS} = \frac{\text{EBIT}}{\text{Sales}}$$

Return on investment (ROI) also called Return on assets (ROA).

It measures the amount of profit generated on investment in assets.

$$\text{ROI/ROA} = \frac{\text{EBIT}}{\text{Total Assets}}$$

Total Assets

Return of equity (ROE):-

It measures the rate of return realized by a firm's stockholders on their investment and serves as an indicator of management performance. ROE measures the return earned on the owner's investment.

$$\text{Return on equity (ROE)} = \frac{\text{EBIT}}{\text{Equity}}$$

Equity

This ratio indicates how well the firm has used the resources of owners. Thus, this ratio is of great interest to present as well as prospective shareholders and also of great concern to management, which has the responsibility of maximizing the owner's welfare.

Operating Efficiency:

It is determined by three variables: sales efficiency (SALEFF), income efficiency (INEFF), and asset turnover (AT) which refer to sales per employee, EBIT per employee, and sales to assets, respectively.

$$\text{Sales efficiency} = \frac{\text{Sales}}{\text{Employee}}$$

Employee

Income efficiency = $\frac{\text{EBIT}}{\text{Employee}}$

Employee

Asset turnover = $\frac{\text{Sales}}{\text{Assets}}$

Assets

This ratio shows the firm's ability in generating sales from all financial resources committed to total assets.

Liquidity:

It is measured by current ratio.

Current Ratio:-is a measure of a firm's short-term solvency

Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liability}}$

Current Liability

Leverage:

This is measured by the ratios of total debt to total assets and debt to equity. It refers to use of fixed costs in an attempt to increase profitability.

Debt Ratio: - measures the extent to which the firm using borrowed.

$$\text{Debt ratio} = \frac{\text{Total Liabilities}}{\text{Total Assets}}$$

Debt-to-Equity Ratio: - measures the proportion of debt capital in terms of equity capital.

$$\text{Debt-to-Equity Ratio} = \frac{\text{Total Liabilities}}{\text{Equity}}$$

Capital investment spending:

This is measured by two ratios:

- Capital expenditure divided by sales

$$= \frac{\text{Capital Expenditure}}{\text{Sales}}$$

- Capital expenditure divided by total assets

$$= \frac{\text{Capital Expenditure}}{\text{Total Assets}}$$

Employment:

It is measured as the total number of employees (EMPL).

CHAPTER FOUR

Findings and Discussion

The purpose of this study is to evaluate the impact of privatization on the financial and operating performance of SOEs. The study is based on comparing different financial and operating performance criteria and ratios of firms in the Leather sub sector in the pre-privatization and post-privatization eras. These criteria include profitability, operating performance, liquidity, leverage, employment and capital expenditure.

In order to analyze the performance of SOEs, the year of privatization was assigned a zero value and the average ratios of the company's performance were calculated. Data were obtained from the annual financial reports of Leather factories four years before and four years after privatization. Performance criteria were calculated and compared to determine whether there are significant differences among them in the pre- and post-privatization periods.

4.1 Enterprise Performance

It is the fact that privatization improves the performance of enterprises in terms of profitability, productivity and capital expenditure, liquidity, leverage and etc Baboukri and Cosset (1998). As stated in the introduction part the objectives of privatization clearly resumes this idea as pointed out by the Ethiopian Privatization Agency and also the concept thoroughly argued by different scholars as per their empirical literatures.

4.1.1. Profitability

Profitability, as defined by several proxies including return on sales, return on assets and return on equity ratios, is assumed to increase post privatization due to change in the enterprise ownership.

Privatization leads the manager to focus on profit goals because under private ownership, the management is directly supervised by shareholders, Vickers and Yarrow (1991). That is why it is expected that the change in ownership from public to private will result in an increase in the profitability of the enterprise. Moreover, they argue that benefits of private ownership stem from the assumption that shareholders will not expropriate investments of manager in the company's assets while the government could re-deploy the investments to serve social goals. The managers then show a greater interest for profits and efficiency in private ownership relative to state ownership. By so doing privatization subjects managers to the pressure of the financial markets and to the monitoring and discipline of profit oriented investor.

4.1.2. Operating Efficiency

Operating Efficiency, as determined by three variables: sales efficiency, income efficiency, and asset turnover, is expected to increase after privatization. This comes about through proper allocation of resources.

As quoted by Getachew (2003), following the transfer of ownership from public to private investors, firms should employ their human, financial and technological resources more efficiently because of a greater stress on profit goals and a reduction of government

subsidies (Kikeris, Nellis and Shirley, 1992; Boycko, Shleifer and Vishny, 1996). In addition, Earle and Telegdy (2002) find that privatization increases labor productivity growth in their heterogeneous sample of Romanian firms and Ehrlich et al. (1994) use a sample of twenty-three comparable international airlines of different ownership categories over the period 1973-83. Their results suggest that private ownership leads to higher rates of productivity growth.

4.1.3. Liquidity

Liquidity, as measured by the ratio of current asset to current liability, is expected to improve in the period following privatization. In developing countries, most of the findings on assessment of financial performance before and after privatization concluded that privatization improves the performance of the enterprise particularly a significant increase in liquidity ratio (Kikri and Nellis, 2004).

In the same vein Pinheiro (1996) studied the impact of privatization on financial performance in Brazil. The research analyzed the financial performance of 50 privatized enterprises before and after privatization, using data during 1990 to 1994. The result of the research confirmed that privatization brings a significant improvement on the financial performance of the privatized enterprises specifically in liquidity.

4.1.4. Leverage

Leverage, as measured by the ratios of total debt to total assets and debt to equity, is expected to decrease after privatization. Many scholars believe that leverage is reduced following privatization due to a combination of greater retained earnings and new share

offerings. Megginson et al. (1994) in a large scale and more comprehensive research compared the pre and post- privatization performance of 61 enterprises in 18 countries, out of which 12 were from developed countries and 6 from developing ones, in 32 industries that experienced full or partial privatization through public share offerings during the period 1961-1990. The result of this research indicates the most enterprises witnessed a significant decrease in leverage.

4.1.5. Capital Expenditure

Capital investment spending, as measured by two ratios: capital expenditure divided by sales and capital expenditure divided by total assets, is also expected to improve after privatization. In their survey article, Megginson and Netter (2001), report that almost all of the twenty-two studies from non-transition economies that they review find that capital investment spending increases significantly as firms are privatized. Perhaps surprisingly, they report that these studies are far less common regarding the impact of privatization on employment levels in privatized firms. It is also, La Porta and Lopez-De-Silanes (1999), in their study of 233 privatized Mexican firms, find that ratios of investment to sales and investment to fixed assets significantly increase after privatization while employment significantly decreases.

In addition as stated by Getachew (2003), often the conditions of privatized state owned enterprises are old and require investment injection to make them operate in a competitive market environment. In addition, Governments expect that greater emphasis on efficiency will lead the newly privatized firms to increase its capital investment spending. Once privatized, the firm should also increase its capital expenditures because

it has greater access to private debt and equity markets and it will have more incentives to invest in growth opportunities (Megginson, Nash and Van Randenborgh, 1994).

4.1.6. Employment

Employment, measured as the total number of employees, is also expected to decrease after privatization though the literature documents that the effect of privatization on employment is ambiguous. Some researchers (Megginson *et al.*, 1994 and Boubakri and Cosset, 1998) report an increase in employment after privatization while (Harper, 2001) find a significant decline in the number of employees after privatization.

In short, profitability, productivity, capital investment, liquidity, and leverage measurements are the most commonly used to assess the performance impact of privatized enterprises. These measurements are equally valuable and very relevant means in evaluating the performance of privatized enterprises.

4.2. Empirical Results

4.2.1 Profitability

Return on sales, return on asset and return on equity are the indicators used to measure profitability. Table (1) summarizes these profit performance indicators.

Table 1: The Results of Profitability Ratios before and after Privatization

Indicator	Mean value before privatization	Mean value after privatization	Mean Change Due to privatization	Percentage of Change	Change Description
Return on Sales	6.48	-2.53	-9.01	-139.04	negative
Return on Asset	9.09	-0.23	-9.32	-102.53	negative
Return on Equity	18.51	2.93	-15.58	-84.17	negative

Source: Descriptive statistics results from selected leather industries financial statement

Table (1) shows a negative effect on return on sales, return on asset, and return on equity after privatization was introduced with mean values of -9.01, -9.32, and -15.58, respectively. In other words, all of the stated profitability proxies return on sales, return on asset and return on equity have relatively larger negative decreases. Return on sales changed from an average of 6.48 before privatization to one of -2.53 after it. Return on asset shifted from an average of 9.09 before privatization to -0.23 after privatization. Similarly, return on equity decreased from an average of 18.51 in the years before privatization to 2.93 in the period following it.

Based on the above three profitability indicators, the results show that privatization does not lead to profit increase in SOEs in the Leather sub sector.

- **Company wise analysis**

- **Profitability**

Table 1.1 Company wise analysis by profitability

Profitability				
	+1	+2	+3	+4
• Universal Leather				
➤ ROA	-0.05	-0.03	-0.05	-0.00
➤ ROS	-0.15	-0.09	-0.11	-0.00
➤ ROE	-0.05	-0.04	-0.06	-0.00
• Modjo Tannery	+1	+2	+3	+4
➤ ROA	-0.12	0.00	0.08	0.13
➤ ROS	-0.26	0.00	0.07	0.11
➤ ROE	-0.36	0.01	0.37	0.73
• Tikur Abay Tannery	+1	+2	+3	+4
➤ ROA	-0.01	0.04	0.09	0.13
➤ ROS	-0.04	0.04	0.05	0.06
➤ ROE	-0.02	0.06	0.14	0.21
• Ethio Tannery	+1	+2	+3	+4
➤ ROA	-0.04	-0.03	0.01	0.02
➤ ROS	-0.04	-0.03	0.01	0.02
➤ ROE	-0.05	-0.04	0.01	0.03
• Awash Tannery	+1	+2	+3	+4
➤ ROA	0.03	0.02	-0.01	0.03
➤ ROS	0.06	0.04	-0.01	0.05
➤ ROE	0.03	0.02	-0.01	0.03
• Ethiopian Pickling & Tanning	+1	+2	+3	+4
➤ ROA	-0.02	-0.12	-0.29	-0.03
➤ ROS	-0.03	-0.21	-0.28	-0.13
➤ ROE	-0.02	-0.12	-0.29	-0.03
• Addis Ababa Tannery	+1	+2	+3	+4
➤ ROA	0.05	0.01	0.05	0.05
➤ ROS	0.05	0.02	0.04	0.04
➤ ROE	0.08	0.02	0.09	0.08

Source- Descriptive statistics results from selected leather industries financial statement

As can be seen from Table 1.1 the results concerning profitability showed that enterprises that are transferred to the private sector show an increasing trend in the first four post privatization periods particularly in the case of Modjo, Tikur Abay, and Ethio Tannery. In addition there is a loss reduction after privatization in Universal Tannery. Even though the results in the industry analysis above showed a decline in profitability performance, the experiences in the privatized enterprises have shown there is an improvement in financial performance in the consecutive years after privatization. But this result is consistent with Baboukri and Cosset (1998). As he analyzed the financial performance of 79 privatized enterprises in 21 developing countries between 1980 and 1992 and found significant increase in profitability, operating efficiency, capital investment, employment and decline in leverage.

4.2.2. Operating Performance

This indicator measures management and employees efficiency in using the available resources. Assets turnover, sales efficiency and income efficiency were the primary indicators of operating performance used. Table (2) shows the mean values of operating performance indicators before and after privatization. Income efficiency and assets turnovers show negative changes with mean values of -5.37 and -0.23, respectively. In other words, income efficiency decreased from an average of 6.57 before privatization to 1.2 after privatization while assets turnover decreased from an average of 1.09 before privatization to 0.86 after privatization. However, sales efficiency shows positive changes before and after the privatization with mean value of 0.33. More specifically,

sales efficiency increased from an average of 1.05 before privatization to one of 1.38 in the years after privatization.

Table 2: The Results of Operating Performance Ratios before and after Privatization

Indicator	Mean value before privatization	Mean value after privatization	Mean Change Due to privatization	Percentage of the change	Description of the change
Assets Turnover	1.09	0.86	-0.23	-21.1	negative
Sales Efficiency	1.05	1.38	0.33	31.43	positive
Income Efficiency	6.57	1.20	-5.37	-81.74	negative

Source: Descriptive statistics results from selected leather industries financial statement

The results show that privatization has a positive effect on sales efficiency before and after privatization. But, it has a negative effect on assets turnover and income efficiency. Thus, from an operational performance perspective, the results partially support the empirical literature that privatization does not have a positive effect on firm performance.

- Company wise analysis

- Operating efficiency

Table 2.1 Company wise analysis by operating efficiency

Operating efficiency				
• Universal Leather	+1	+2	+3	+4
➤ Income efficiency	-3.51	-2.27	-3.26	-0.05
➤ Asset turnover	0.34	0.38	0.46	0.46
• Modjo Tannery	+1	+2	+3	+4
➤ Income efficiency	-16.47	0.53	17.53	34.53
➤ Asset turnover	0.45	0.84	1.09	1.26
• Tikur Abay Tannery	+1	+2	+3	+4
➤ Income efficiency	-1.27	3.89	9.06	14.22
➤ Asset turnover	0.37	1.09	1.74	2.32
• Ethio Tannery	+1	+2	+3	+4
➤ Income efficiency	-7.84	-7.11	1.74	5.18
➤ Asset turnover	1.02	1.10	1.08	1.11
• Awash Tannery	+1	+2	+3	+4
➤ Income efficiency	6.34	3.85	-2.65	6.38
➤ Asset turnover	0.49	0.39	0.80	0.54
• Ethiopian Pickling & Tanning	+1	+2	+3	+4
➤ Income efficiency	-3.23	-14.61	-25.50	-3.88
➤ Asset turnover	0.73	0.58	1.03	0.27
• Addis Ababa Tannery	+1	+2	+3	+4
➤ Income efficiency	6.60	1.88	7.42	6.12
➤ Asset turnover	0.92	0.67	1.22	1.25

Source- Descriptive statistics results from selected leather industries financial statement

Despite the fact that, from an operational performance perspective, the results of industry analysis revealed that privatization has an adverse effect on firm performance due to income efficiency and asset turnover negative change in means after the period following privatization; some privatized enterprises results have shown that there is a step up in operating efficiency in the consecutive years after privatization. As Table 2.1 reveals the results relating to operating efficiency showed that enterprises that are transferred to the private sector show a growing trend in the first four post privatization periods particularly in the case of Modjo, Tikur Abay, and Ethio Tannery. In addition there is an improvement after privatization in the Universal Tannery since the trend shows that income efficiency values go to the least negative values. The company analysis results consistent with Pinheiro (1996). He studied the impact of privatization on financial performance in Brazil. The research analyzed the financial performance of 50 privatized enterprises before and after privatization, using data during 1990 to 1994. The result of the research confirmed that privatization brings a significant improvement on the financial performance of the privatized enterprises.

4.2.3. Liquidity

The indicator current ratio is used to measure liquidity, as shown in Table (3).

Table 3: The Results of Liquidity Ratios before and after Privatization

Indicator	Average before privatization	Average after privatization	Average Change	Percentage of Change	Change Description
Current ratio	1.76	2.99	1.23	69.89	positive

Source: Descriptive statistics results from selected leather industries financial statement

Table (3) depicts that liquidity affects privatization positively based on calculations of current ratio. Current ratio was found to rise from an average of 1.76 in the years before privatization to 2.99 in the period after it with positive mean value of 1.23. This indicates that current assets exceeded current liabilities after privatization was introduced.

4.2.4. Leverage

Debt to equity and debt to total assets were used as indicators of leverage, for they show the extent to which debt is used in firms capital structure. Table (4) summarizes related results.

Table 4: The Results of Leverage Ratios before and after Privatization

Indicator	Average before privatization	Average after privatization	Change in Average	Percentage of Change	Change Description
Debts to Equity	95.05	77.03	- 18.02	- 18.96	positive
Debts to assets	44.49	30.15	- 14.34	- 32.23	positive

Source: Descriptive statistics results from selected leather industries financial statement

The ratio of debt to equity was found to decline from an average of 95.05 before privatization to 77.03 after it. By the same token, the debt to total assets ratio was found to decrease from an average of 44.49 in the period before privatization to 30.15 in the period following it. This indicates that the debt to equity and debt to assets ratios have largely decreased as a result of privatization with mean values of 18.96 and 32.23, respectively. The results show that privatization could lead to debt reduction.

4.2.5. Capital Expenditure

Two ratios capital expenditure to sales and capital expenditure to total assets were used in this category to measure investment spending, as shown in Table (5).

Table 5: The Results of capital expenditure Ratios before and after Privatization

Indicator	Average before privatization	Average after privatization	Average Change	Percentage of Change	Change Descriptio n
Capital expenditure to sales	0.2143	0.2360	0.0217	10.13	positive
Capital expenditure to assets	0.1145	0.1486	0.0341	29.78	positive

Source: Descriptive statistics results from selected leather industries financial statement

Table (5) shows an increase in capital expenditure to sales then from 0.2143 in the years before privatization to 0.2360 in the period after it with a positive average change of 0.0217. Similarly, an increase in capital expenditure to assets from 0.1145 before privatization to 0.1486 after privatization with a positive average change of 0.0341. This depicts that privatization leads to capital expenditure increment immediately after privatization.

4.2.6. Employment

Employment is an important and critical issue in privatization because of the possibility that privatization could lead to cutting the current level of employment. There is neither a theoretical nor an empirical consensus concerning the impact of privatization on employment.

Table 6: The Results of employment data before and after Privatization

Indicator	Average before privatization	Average after privatization	Average Change	Percentage of Change	Change Description
Number of employees	3298	3085	-213	-6.46	negative

Source: Descriptive statistics results from selected leather industries financial statement

The result show that employment decreases after privatization. The average number of employees was found to decline from 3298 to 3085 employees after privatization, which means that SOEs in the Leather sub sector may have been overstaffed in the years preceding privatization.

Table 7 - Post privatization actual performance Vs Expected results

Performance indicators	Expected Outcome	Actual Outcome
1. Profitability <ul style="list-style-type: none"> • Return on asset • Return on sales • Return on equity 	Increase Increase Increase	Decrease Decrease Decrease
2. Operating efficiency <ul style="list-style-type: none"> • Sales efficiency • Income efficiency • Asset turnover 	Increase Increase Increase	Increase Decrease Decrease
3. Liquidity <ul style="list-style-type: none"> • Current ratio 	Increase	Increase
4. Leverage <ul style="list-style-type: none"> • Debt to asset • Debt to equity 	Decrease Decrease	Decrease Decrease
5. Capital investment <ul style="list-style-type: none"> • Capital expenditure to sales • Capital expenditure to asset 	Increase Increase	Increase Increase
6. Employment <ul style="list-style-type: none"> • No of employees 	Decrease	Decrease

Source – As per the empirical results of above analyzed data.

4.3 Result Discussion

4.3.1 Profitability

As Table 1 reveals the study results concerning profitability showed that enterprises that are transferred to the private sector show a decline trend in the first four post privatization periods. Despite the fact that performance and profitability is expected to improve in the privatized enterprises, the experiences in the study have shown quite the contrary. But this result is consistent with Harper (2001) documents different findings for 178 Czech firms that were included in the first wave of voucher privatization. He concludes that profitability and efficiency decrease immediately following privatization.

It is true that very difficult to propose the main reasons for the decline in profitability after the period following privatization in the Leather sub sector. But the officials of post privatization impact assessment team during the informal interview indicated that firms in the sector faced unexpected government policy shift immediately after privatization. As per the team leader, Ato Duna, the policy depicts that companies in the leather industry must produce semi and finished leather products relative to firms primary output is a raw product before privatization. This fact hindered the firms' competitive advantage and market development in the tough competitive leather market. Likewise the firms were forced to change their production systems by new machineries, and train their workers and develop the management with the new technology process system without enough preparation and assessment of the market for survival, hence the cost of production was higher while producing semi and finished type of products. In addition

shortage of qualified workers and professionals in the market are the major source of declining in profitability.

According to Getachew (2003) the fall in profitability, among other thing, is explained by high cost of production and severe unhealthy competition that resulted from trade liberalization and openness. In addition, he pointed out that the introduction of high depreciation cost due to high price of asset evaluation upon privatization, have also exaggerated the enterprise loss. Buyers complain that they paid very high price for very old and out dated machines. This has inflated the cost of depreciation and hence increased production cost, which in turn has limited their competitive power in a free market environment.

Even if the study results consistent with the above empirical literatures in connection with profitability performance indicator, it is contrasted with Baboukri and Cosset (1998) result. As they analyzed the financial performance of 79 privatized enterprises in 21 developing countries between 1980 and 1992 and found significant increase in profitability, operating efficiency, capital investment, employment and decline in leverage.

4.3.2 Operating Efficiency

As can be seen from Table 2, from an operational performance perspective, the results partially support the empirical literature that privatization does have a positive effect on firm performance. This is resulted from sales efficiency positive change in mean after the period following privatization but negatively resulted in light of income efficiency and

asset turnover. The study outcome consistent with mixed empirical results. Martin and Parker (1995) find mixed results in performance -in terms of profitability and efficiency- for 11 privatized firms in the UK. Likewise some recent studies control for unobserved firm heterogeneity using firm fixed effects in a panel data analysis (Earle and Telegdy, 2002; Wallsten, 2001)⁴. The results of these studies on privatization and firm performance are mixed.

The improvement in productivity in light of sales efficiency, which is 33 percent for means, among other things, is explained by a reduction in the number of employees with a considerable increase in sales and it is also improved due to considering parameter values before the cost of production made in the calculation of its ratio. Whereas higher cost of production after privatization decline return values which in turn restrict income efficiency as per employee performance. In addition the other main source of negative mean value of income efficiency was high depreciation cost. Getachew (2003), pointed out that the introduction of high depreciation cost due to high price of asset evaluation upon privatization, have also exaggerated the enterprise loss. Similarly Frydman et al. (1999), find that privatization to outsider owners has significant effects on revenue performance, but not on cost reduction using data from the Czech Republic, Hungary and Poland, of 218 state owned firms, of which 128 were privatized during the period from 1990 to 1994.

⁴ See Cagla Okten and et al; [2005]: the Effects of Privatization on Efficiency: How Does Privatization Work, Bilkent University, Department of Economics, Ankara, Turkey.

Similarly with income efficiency, asset turnover results negative mean change but the reason here was higher capital investment in the period after privatization in order to improve process system in light of technology. In addition limited competitive ability within the market due to poor quality of semi and finished leather products. This has decreased the sales of the companies and hence decreased asset turnover, which in turn has limited their efficiency relative to pre privatization.

4.3.3 Liquidity

As depicted in Table 3 the results specify that current assets highly exceeded current liabilities after privatization was introduced, which indicates an evident improvement in performance after privatization, probably leading to liquidity improvement in the Leather sub sector. The study result consistent with the expected outcome and also it is supported by Kikri and Nellis, (2004). Their findings on assessment of financial performance before and after privatization concluded that privatization improves liquidity ratio significantly.

It is evidenced that after privatization most of the private owners use their own source for the working capital needs of the organization. Ato Seifu, one of the officials in pre privatization office, said that private owners are not interested to use short term loans though his office encouraged them since their current ratio far from the standard one. But most of them did not accept the idea since they feared to use debt financing in the short run. The reasons mentioned here are the privatized firms had no a good will in their past track of record and high cost of debt. This condition forced owners to use equity financing to finance the operations in the short run.

4.3.4 Leverage

As Table 4 indicates the debt to equity and debt to assets ratios have largely decreased as a result of privatization with mean values of 18.96 and 32.23, respectively. The results show that privatization could lead to debt reduction. Privatization might decrease a firm's degree of financial leverage as the cost of debt will be higher for a privatized firm compared to an SOE, given that the public sector has the advantage of paying a lower interest rate on debt. On the other hand, privatized firms have more opportunities to access equity markets domestically and internationally (Bradley, Jarrell, and Kim, 1984).⁵

As cited in Mohammed (2004) such results are consistent with Kocenda and Svejnar's (2002) findings as they document that majority state-ownership are associated with linearly declining financial leverage. The argument here is that the government might try to carry out strategic restructuring by reducing the debt ratio to be able to sell the remaining stakes of the partially privatized firms.

In connection with the above fact most of the private owners claimed that unable to get long term loans from the financial institutions since the privatized firms had no a good will in their past track of record, high cost of debt and also many of the fixed assets like machineries are not in best position to use them as a collateral. In connection with the last mentioned reason most of the buyers complain that they paid very high price for very old

⁵ See Mohammed Omran; [2004] : Performance Consequences of Privatizing Egyptian State Owned Enterprises: The Effect of Post-Privatization Ownership Structure on Firm Performance, Arab Academy for Science & Technology, College of Management & Technology, Alexandria.

and out dated machines. This has inflated the cost of depreciation and hence has limited their competitive advantage in getting loans, Getachew (2003).

In addition it is the fact that most of commercial banks are not interested to grant loans to them particularly long term loans since the ceiling of loan rate is not attractive for banks as a finance company and hence has shifted to invest in different investment securities which in turn limits enterprise owners to access loans.

4.3.5 Capital Expenditure

As can be seen from Table 5 the result reveals that there is an increase in capital investment spending as expected. In this study, investment intensity is captured by two proxies: Capital expenditure to Sales, and Capital expenditure to Total assets. Both results show increases in all ratios. Moreover, in a situation where there are old and highly depreciated enterprises, an immediate initiative through investment injection would become imperative to coup up with a market competitive environment. Following privatization, often managers are forced to make necessary adjustments that may require change in product mix, improve efficiency and optimal allocation of resources through new capital spending.

As mentioned in the profitability analysis, privatized firms have been forced to produce semi and finished leather products instead of raw products by the government in the period after privatization. This fact led firms to adopt new processing machineries as per the existing technology. It can be considered as one of the major source of an increase in capital investment.

In addition private investors tried to make an improvement by doing away with machinery, equipment and installations that are obsolete or could not be used efficiently after privatization. The general trend and the results observed so far are consistent with those documented by Megginson, Nash and Van Randenborgh, (1994) that suggests that privatization, will induce incentives to invest in newly privatized firms.

4.3.6 Employment

Table 6 revealed that employment decreases after privatization which means that SOEs in the Leather sub sector may have been overstaffed in the years preceding privatization. The study output consistent with expected and empirical. La Porta and Lopez-De-Silanes (1999) find that ratios of investment to sales and investment to fixed assets significantly increase after privatization while employment significantly decreases.

A decline in total number of employees is insignificant due to the legal agreement between the privatized firm and the authorized agency. As per the officials of post privatization agency, there is a mutual agreement in the status of employment. The legal document reveals that the firm has an obligation to maintain existing employees as is otherwise compensate them while layoff since the privatized firms abide by the law.

However, the above view needs to be elaborated by further study as it is beyond the scope of this paper and hence it is very hard to boldly conclude it as the main reason contributing to the performance of privatized enterprises. This may require long time observation beyond four years.

CHAPTER FIVE

Summary, Conclusions and Recommendation

5.1 Summary of findings and conclusions

The objective of this study is to examine the impact of privatization on financial and operating performance of Leather factories in its sub sector by using both descriptive and quantitative ratio analysis. In order to achieve this objective, the study addressed the theoretical aspects of privatization, by reviewing concepts, objectives, methods, impacts, and experiences of some countries, particularly developing countries. Furthermore, the study concentrated on Ethiopian privatization experience, which serves to establish a framework for the study and to derive the variables essential for conducting this examination.

A sample of 7 enterprises is carefully selected from 9 privatized enterprises which have at least four years data in the Leather industry. Two were left since one is due to unavailability of pre data where as the other due to it is privatized recently. For each enterprise twelve financial performance indicators are calculated as average of four years before, and four years after privatization. The twelve indicators are grouped into six standard broad categories: profitability (3 indicators); operating efficiency (3 indicators), Liquidity (one indicator); leverage (two indicators); capital investment spending (two indicators) and employment one indicator.

To examine the performance of firms in Leather sub sector, the study followed the standard methodology of comparison used in the literature and empirical studies to compare the pre- and post- privatization financial and operating performance of the company that experienced full privatization through selling the government shares in the stated sub sector.

The result of the study revealed that there were positive improvements in the performance of SOEs after privatization in terms of liquidity and debt ratios compared to its performance before privatization.

The performance indicators showed also an increase in sales efficiency. On the other hand, the operation performance indicator of asset turnover, and income efficiency was decreased.

To determine whether privatization had an impact on the financial and operating performance of the SOEs in Leather sub sector in light of profitability the study compared profitability indicators of the company. The results revealed a decrease in profitability.

The study also confirmed that there was an increase in capital investment as per the results of the capital expenditure to sales and capital expenditure to assets ratio where as employment was declined.

In conclusion, the results suggest that privatization has negative effects on firm performance in the leather sub sector. It is found that profitability, and efficiency except sales efficiency of privatized firms decline after privatization. In addition, the study

documents a decline in leverage as measured by total debt to total assets or debt to equity of firms in the post-privatization period and an improvement in liquidity performance. Remarkably, there is a decline in employment in the years following privatization. Finally, the findings confirm that privatization results in an increase in capital expenditure after privatization. In general the results go against the empirical literature that states privatization improves the performance of privatized companies in terms of profitability and operating efficiency.

While the causes of such disappointing outcome must expect further empirical analysis, using an appropriate methodology, there is evidence to suggest that such causes may include: inadequate finance, increases in production costs, low employees and management efficiency and assets valuation error up on privatization.

5.2 Recommendations

Finally, I tried to provide a set of some recommendations

- Firms should give high attention on employee training and management development through providing access to different training programs.
- Privatized enterprises should give more emphasis on cost control.
- Better use of professionals while valuing enterprises asset up on privatization.
- Efforts should be directed to developing the capital market to overcome the problem of finance.

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Appendix 1

Profitability Performance of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Profitability Proxy - ROS

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.0678	-0.086	-0.1538	-2.26844
2.	Awash Tannery Factory	0.1914	0.0345	-0.1569	-0.81975
3.	Ethiopian Pickling and Tanning Factory	0.0874	-0.162	-0.2494	-2.85355
4.	Addis Ababa Tannery S.C	0.0878	0.0386	-0.0492	-0.56036
5.	Modjo Tannery S.C	-0.0789	-0.0195	0.0594	-0.75285
6.	Tikur Abay Shoe S.C	0.0756	0.0275	-0.0481	-0.63624
7.	Ethiopia Tannery S.C	0.0225	-0.0102	-0.0327	-1.45333
	Mean	0.0648	-0.0253	-0.0901	-1.39043

Profitability Proxy - ROA

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.0637	-0.0332	-0.0969	-1.52119
2.	Awash Tannery Factory	0.2982	0.0153	-0.2829	-0.94869
3.	Ethiopian Pickling and Tanning Factory	0.1654	-0.1165	-0.2819	-1.70435
4.	Addis Ababa Tannery S.C	0.0727	0.0405	-0.0322	-0.44292
5.	Modjo Tannery S.C	-0.0539	0.0246	0.0785	-1.4564
6.	Tikur Abay Shoe S.C	0.0735	0.0633	-0.0102	-0.13878
7.	Ethiopia Tannery S.C	0.0167	-0.0105	-0.0272	-1.62874
	Mean	0.0909	-0.0023	-0.0932	-1.0253

Profitability Proxy - ROE

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.1195	-0.0387	-0.1582	-1.32385
2.	Awash Tannery Factory	0.7861	0.0169	-0.7692	-0.9785
3.	Ethiopian Pickling and Tanning Factory	0.3099	-0.1178	-0.4277	-1.38012
4.	Addis Ababa Tannery S.C	0.1332	0.0697	-0.0635	-0.47673
5.	Modjo Tannery S.C	-0.19	0.1896	0.3796	-1.99789
6.	Tikur Abay Shoe S.C	0.1142	0.0964	-0.0178	-0.15587
7.	Ethiopia Tannery S.C	0.0223	-0.0112	-0.0335	-1.50224
	Mean	0.1851	0.0293	-0.1558	-0.84171

Appendix 2

Operating Efficiency Performance of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Operating Efficiency Proxy – Sales Efficiency

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	25.02	27.96	2.94	0.117506
2.	Awash Tannery Factory	137.22	126.11	-11.11	-0.08096
3.	Ethiopian Pickling and Tanning Factory	114.91	72.45	-42.46	-0.36951
4.	Addis Ababa Tannery S.C	74.28	137.47	63.19	0.8507
5.	Modjo Tannery S.C	111.37	195.61	84.24	0.756398
6.	Tikur Abay Shoe S.C	64.97	138.45	73.48	1.130984
7.	Ethiopia Tannery S.C	204.56	271.25	66.69	0.326017
	Mean	104.62	138.47	33.85	0.323552

Profitability Proxy - ROE

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.1195	-0.0387	-0.1582	-1.32385
2.	Awash Tannery Factory	0.7861	0.0169	-0.7692	-0.9785
3.	Ethiopian Pickling and Tanning Factory	0.3099	-0.1178	-0.4277	-1.38012
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6.	Tikur Abay Shoe S.C	0.1142	0.0964	-0.0178	-0.15587
7.	Ethiopia Tannery S.C	0.0223	-0.0112	-0.0335	-1.50224
	Mean	0.1851	0.0293	-0.1558	-0.84171

Appendix 2

Operating Efficiency Performance of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Operating Efficiency Proxy – Sales Efficiency

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	25.02	27.96	2.94	0.117506
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4.	Addis Ababa Tannery S.C	74.28	137.47	63.19	0.8507
5.	Modjo Tannery S.C	111.37	195.61	84.24	0.756398
6.	Tikur Abay Shoe S.C	64.97	138.45	73.48	1.130984
7.	Ethiopia Tannery S.C	204.56	271.25	66.69	0.326017
	Mean	104.62	138.47	33.85	0.323552

Operating Efficiency Proxy – Income Efficiency

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	1.86	-2.28	-4.14	-2.22581
2.	Awash Tannery Factory	25.56	3.48	-22.08	-0.86385
3.	Ethiopian Pickling and Tanning Factory	10.12	-11.8	-21.92	-2.16601
4.	Addis Ababa Tannery S.C	7.16	5.5	-1.66	-0.23184
5.	Modjo Tannery S.C	-7.69	9.03	16.72	-2.17425
6.	Tikur Abay Shoe S.C	4.96	6.48	1.52	0.306452
7.	Ethiopia Tannery S.C	4.01	-2.01	-6.02	-1.50125
	Mean	6.57	1.2	-5.37	-0.81735

Operating Efficiency Proxy – Asset Turnover

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.885	0.41	-0.475	-0.53672
2.	Awash Tannery Factory	1.6	0.56	-1.04	-0.65
3.	Ethiopian Pickling and Tanning Factory	1.64	0.65	-0.99	-0.60366
4.	Addis Ababa Tannery S.C	0.752	1.02	0.268	0.356383
5.	Modjo Tannery S.C	0.894	0.91	0.016	0.017897
6.	Tikur Abay Shoe S.C	0.951	1.38	0.429	0.451104
7.	Ethiopia Tannery S.C	0.907	1.08	0.173	0.190739
	Mean	1.09	0.86	-0.23	-0.21101

Appendix 3

Liquidity Status of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Liquidity Proxy – Current Ratio

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	1.7	3.84	2.14	1.258824
2.	Awash Tannery Factory	1.42	4.51	3.09	2.176056
3.	Ethiopian Pickling and Tanning Factory	1.72	2.29	0.57	0.331395
4.	Addis Ababa Tannery S.C	1.42	2.36	0.94	0.661972
5.	Modjo Tannery S.C	1.17	2.17	1	0.854701
6.	Tikur Abay Shoe S.C	2.17	2.6	0.43	0.198157
7.	Ethiopia Tannery S.C	2.74	3.17	0.43	0.156934
	Mean	1.76	2.99	1.23	0.698864

Appendix 4

Leverage Status of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Leverage Proxy – Debt to Equity

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.807	0.185	-0.622	-0.77076
2.	Awash Tannery Factory	1.62	0.079	-1.541	-0.95123
3.	Ethiopian Pickling and Tanning Factory	0.722	0.011	-0.711	-0.98476
4.	Addis Ababa Tannery S.C	0.795	0.721	-0.074	-0.09308
5.	Modjo Tannery S.C	1.93	3.28	1.35	0.699482
6.	Tikur Abay Shoe S.C	0.488	0.54	0.052	0.106557
7.	Ethiopia Tannery S.C	0.292	0.578	0.286	0.979452
	Mean	0.9505	0.7703	-0.1802	-0.18958

Leverage Proxy – Debt to Asset

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.442	0.1506	-0.2914	-0.65928
2.	Awash Tannery Factory	0.62	0.071	-0.549	-0.88548
3.	Ethiopian Pickling and Tanning Factory	0.41	0.0107	-0.3993	-0.9739
4.	Addis Ababa Tannery S.C	0.441	0.4188	-0.0222	-0.05034
5.	Modjo Tannery S.C	0.655	0.7546	0.0996	0.152061
6.	Tikur Abay Shoe S.C	0.322	0.3514	0.0294	0.091304
7.	Ethiopia Tannery S.C	0.225	0.3533	0.1283	0.570222
	Mean	0.4449	0.3015	-0.1434	-0.32232

Appendix 5

Capital Investment Status of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Capital investment Proxy – Capital Expenditure to Sales

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.1955	0.2397	0.0442	0.226087
2.	Awash Tannery Factory	0.1219	0.1989	0.077	0.631665
3.	Ethiopian Pickling and Tanning Factory	0.1758	0.5761	0.4003	2.277019
4.	Addis Ababa Tannery S.C	0.2964	0.2759	-0.0205	-0.06916
5.	Modjo Tannery S.C	0.3955	0.2939	-0.1016	-0.25689
6.	Tikur Abay Shoe S.C	0.1892	0.0216	-0.1676	-0.88584
7.	Ethiopia Tannery S.C	0.1264	0.0456	-0.0808	-0.63924
	Mean	0.2143	0.236	0.0217	0.10126

Capital investment Proxy – Capital Expenditure to Asset

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	0.1698	0.0964	-0.0734	-0.43227
2.	Awash Tannery Factory	0.1916	0.1035	-0.0881	-0.45981
3.	Ethiopian Pickling and Tanning Factory	0.1139	0.3028	0.1889	1.658472
4.	Addis Ababa Tannery S.C	0.1162	0.2616	0.1454	1.251291
5.	Modjo Tannery S.C	0.1532	0.2089	0.0557	0.363577
6.	Tikur Abay Shoe S.C	0.0134	0.018	0.0046	0.343284
7.	Ethiopia Tannery S.C	0.043	0.0489	0.0059	0.137209
	Mean	0.1145	0.1486	0.0341	0.297817

Appendix 6

Employment Status of Selected Privatized Enterprises in the Leather Sub sector before and after Privatization

Employment Proxy – No. of Employees

No.	Enterprises	Average Before Privatization	Average After privatization	Mean Change After- Before	Performance Rate
1.	Universal Leather Articles Factory	317	271	-46	-0.14511
2.	Awash Tannery Factory	757	720	-37	-0.04888
3.	Ethiopian Pickling and Tanning Factory	363	292	-71	-0.19559
4.	Addis Ababa Tannery S.C	318	264	-54	-0.16981
5.	Modjo Tannery S.C	231	290	59	0.255411
6.	Tikur Abay Shoe S.C	542	465	-77	-0.14207
7.	Ethiopia Tannery S.C	770	783	13	0.016883
	Total	3298	3085	-213	-0.06458

Appendix 7

Privatized Companies

Name of Enterprises	Year of Privatization
Universal Leather Articles Factory	1998
Awash Tannery Factory	1998
Ethiopian Pickling and Tanning Factory	1998
Addis Ababa Tannery S.C	2006
Modjo Tannery S.C	2006
Tikur Abay Shoe S.C	2006
Ethiopia Tannery S.C	2006

Source- Ethiopia Privatization Agency (EPA)