Impact of privatization on Financial and Operating Performance of Privatized Firms

(A case study of Tikur Abay Shoe Share Company)

A Research Project Submitted in Partial Fulfillment of the Requirement for the Award of Master of art degree in Business Administration

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Declaration

I**, Muluken Alemu Haile**, hereby declare that the thesis entitled "**Financial and operating Performance of privatized firms": A case study of Tikur Abay Shoe Share Company**. Submitted by me for the award of the degree of Master of Business Administration to the Collage of Business and Economics, Mekelle University, through the department of Management, is my original work and it has not been presented for the award of any other Degree, Diploma, Fellowship or other similar titles of any other University or institution.

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Certification

This is to certify that this thesis entitled "**Financial and operating Performance of privatized firms"** a case study of **Tikur Abay Shoe Share Company**. Submitted in partial fulfillment of the requirements for the award of the degree of MBA in finance to the College of Business and Economics, Mekelle University, through the Department of Management , done by Mr. Muluken Alemu, Id. No.**FBE/PR0009/01** is an authentic work carried out by him under my guidance. The matter embodied in this thesis has not been submitted earlier for award of any degree or diploma to the best of my knowledge and belief.

Principal advisor: G.C Srinivasa rao (Asst. Professor)

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Co advisor: Samson yemaneh.

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Date……..

Abstract

Although privatization has turned in to world phenomena, it is only recently that Ethiopia has launched privatization programs. This paper compares the financial and operating performance of Tikur Abay Shoe Share Company before and after privatization and it investigates some of the major factors that affect its financial and operating performance. The objective of this paper is comparing the pre and post privatization financial and operating performance of the company so as to check whether there is improvement or decline following privatization.

The data used in this study was obtained from the audited financial statement of the company. Ten financial performance indicators are calculated as average of three years before and three years after privatization .under profitability three ratios (return on sales, return on asset and return on equity),under operating efficiency (sales efficiency and net income efficiency) ,under capital investment(capital expenditure/ total asset and capital expenditure / total sales), employment(total NO. of employees), under leverage(total debt/total asset) and finally under liquidity (current asset/current liability) were considered further more T-test statistics is employed to examine mean differences of each variables before and after privatization.

Contrary to the expectation of the government; the study documented decline in profitability, net income efficiency, capital investment, liquidity and insignificant increment in sales efficiency, leverage and number of employment following privatization. This is because the company has technology and marketing related problems like: Poor product diversification, Weak product distribution system, poor promotion system, lack of experience and skill in designing competitive and fashionable shoe, lack of adequate skill and equipment to conduct quality control, , average age of employees is too high as a result there is high absenteeism, Poor work handling techniques, Poor supervision and Lack of modern technology and machines resulted poor productivity and limited scope of product diversification are some of the major factors that affect its financial and operating performance.

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Muluken Alemu

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Acronyms

TASSCo ……. Tikur Abay Shoe Share Company

CAPEX …….….……..capital expenditure

EPA …….…. Ethiopian privatization agency

EMPL ……..…….. Employment

NIEFF …….……..….. Net income efficiency

SALEFF …….……..sales efficiency

CETA …….….…… capital expenditure to asset

CETSA …… capital expenditure to sales

TDTA ……....…….total debt to total asset

ROS……..……. return on sales

ROA …….…….. Return on asset

ROE …….. Return on equity

SOEs ……..state owned enterprises

WB…….....……World Bank

MNR…….. Megginson, Nash, and Randenborgh

Table of content

Contents **pages**

List of tables

page

List of figures

Page

Chapter I: Introduction

1.1 Background of the study

Privatization is now widespread in industrialized, developing and transitional economies. In the last two decades, countries around the world have embarked on major privatization programs, yet many remain reluctant to privatize while still more have had to halt ongoing processes of privatization. This is particularly true in developing countries, where state-owned Enterprises (SOE) still account for more than 10 percent of gross domestic product, 20 percent of investment and about five percent of formal employment (Kikeri, Nellis, And Shirley, 1994). The aversion to privatization appears to be associated with public distrust of the privatization process. Unions and other traditional opponents of privatization have argued that it results in layoffs and poorer services. Political leaders, meanwhile, fear that the higher profitability of private companies comes at the expense of the rest of society, especially during the difficult transition period from state ownership to private ownership.

Privatization has turned into a major phenomenon for the developed world as well as the developing world. Over the last decade, state-owned enterprises (SOEs) have been privatized at an increasing rate, particularly in developing countries. In this regard, Sader (1993) reports that total privatization proceeds in developing countries rose from $2.6 billion in 1988 to $23.2 billion in 1992. Furthermore, the importance of privatizations in developing countries relative to observed in developed countries increased dramatically. The objectives of privatization are numerous. Country studies show that these objectives include improving government cash flows by reducing subsidies and capital infusions to SOEs, promoting popular capitalism through a wider ownership of shares, restraining the power of trade unions in the public sector, redistributing incomes and rents within society, satisfying foreign donors by reducing the government's role in the economy and especially enhancing the efficiency and the performance of

the SOE sector based on the rationale that the private sector outperforms the public sector (Ramamurti, 1991).

In the modern world of the present time, the economic system of almost all countries, throughout the world, are dominated by organized forms of business organizations. This is particularly true in a free market economic system which is the most prevalent system nowadays after the down fall of the soviet bloc.

Although privatization has turned in to world phenomena, it is only recently that Ethiopia has launched privatization programs. Ethiopia is one of the poorest and least developed country in the world with low per capita income ,high rate of illiteracy, lack of infrastructure, technology and thus need badly a well developed business sector for its economic development .

To this end, the existing government of Ethiopia (federal democratic republic of Ethiopia) design and implement the policy that allows the involvement of private sectors in establishing and expanding business at various sectors. The government has trying to strengthening the operations of state owned business organizations. In addition the government has taken measure to transfer ownership of state owned business firms to private investors. It is one of the key elements of the continuing phenomenon of the increasing use of markets to allocate resources. As a result, from time to time, there has been a tremendous change in country's business environment.

In light of such a policy environment and acute need for the expansion of business, a number of firms have been privatized by the government. During the past decade (1991-2000) the privatization of state-owned enterprises has been moved from being a radical, almost desperate, policy initiative of the government of Ethiopia to bring an accepted economic policy for government of all ideological stripes. Now these organizations are playing an important role in the country's economic development. For instance in 1992 the total sales volume in developing countries ($23.2billon) was for the first time, larger than the revenues generated by privatization in industrialized countries ($17.3 billion) (The Economist, march 1997).

In Ethiopia during the dergue regime, state investment dominated all sectors of the economy of the private sector was deliberately marginalized and neglected. Hence the economic development

of the country lagged behind. Therefore, so as to come up with an alarming economic development and wealth maximization the countries Experience would dictate as a mandatory phenomenon to concentrate private firms than state owned firms. Even if this was a very important issue needs to get an attention of the government, it was ignored for a long period of time until 1991.

However, since 1991, the government of Ethiopia embarked up on privatization of state owned enterprise as integral part of the broader macro economic reform program, in order to implement the program; the government established the privatization agency which empowered to privatize state owned enterprises (proclamation No 87/1994). Through this privatization program, the government aims to concentrate more on policy making and monitoring function, to enhance managerial efficiency, cost effectiveness and innovation in business activity to decrease the budgetary Burdon of the state owned enterprises and to encourage local and foreign investment. (Proclamation No. 146/1998)

The Ethiopian government in line with its commitment to encourage the private sectors has so far taken a broad-based economic reform program. One of the reform measures is a privatization program which has transferred so far over 225 enterprises (EPA, 2001). Few studies have assessed the privatization process and its impact on enterprise in Ethiopia like: Regasa (2003), Hailu (2005) and Simon (2010)

Even though studies are made on this area they simply show the impact of privatization on firms financial and operating performance. But this paper will further investigate some of the major causes that affect the financial and operating performance of the company.

This study was conducted particularly in Tikur Abay Shoe Share Company which is located 10KM far from center of Addis Ababa (the capital of Ethiopia). And the company was privatized by five share holders in the year 2006.

1.2. Background of Tikur Abay Shoe Share Company.

1.2.1 Historical Background of TASSCo.

Tikur Abay Shoe factory was established in 1948.it is located west of the central side of Addis Ababa (capital of Ethiopia), heralded a strategy of conquest founded on the overall mastery of the complex structures of the wear industry: manufacture, trading and distribution of different types of civilian foot wear. This exemplary achievement is constructed on value of perseverance and awareness of customer requirement. It had total land holdings of 49,815mwas holdings of the main factory site while the balance is located in its branches. The factory was initially established by entrepreneurs with a capital of birr 200,000(about USD25, 000 with to date exchange rates) employing 75 people.

It registered growth in the past and registered now birr 22, 053, 000(USD 2,756,000) of net worth fully owned by the government to this end, the factory's attainable capacity is 600,000 pairs of various types of shoe and 200,000 kgs of glue which could be used for its Own use and external markets as well. For this regard the company's current employment is close to 600 employees.

Tikur Abay Shoe Share Company which is backed by half a century of rich experience, is Ethiopia's biggest shoe factory engaged in the production of military and civilian durable leaser footwear all made from genuine leaser utilizing a vulcanization process.

Apart from the production of shoes, TASSCo is engaged in the production of multi purpose glue both for its own use and for the market.

1.2.2Vision, mission and values of TASSCo

Vision

To continue being the leading in the local market as well as to export quality shoes to foreign market by applying modern technologies. In addition to these controlling the local markets by producing and distributing of causal shoes with reasonable price and better quality to the society

Mission

To be profitable in sustainable manner by production and distribution of shoes and multipurpose glue with reasonable price and better quality to the local as well as export market so as to generate foreign currency to the country and to minimize import of similar product by producing substitute products at local in order to save foreign currency**.**

Value

- To satisfy its customers demand by providing convenience and reliable quality shoe.
- Making the shoe company profitable.
- Proper usage of company's asset.
- Proper usage of working hours.
- Enhancing our knowledge at any time.

Business objective of the company

The populations of the company then initiated modern leather industry in Ethiopia 50 years back to meet the then growing demand. To date, circa 4000 peoples were engaged in the sector in about 40 medium and small-scale enterprises.

Most of the raw materials for leather shoe production were of local sources.

The major objective of the company is to produce heavy duty shoes (military, miners, workmen etc) shoes. It is the only company not only in the country but also in the horn of Africa region. Moreover, it does produce other shoe of civilian type for people in different walks of like kids, ladies and gents.

The company's net worth is divided in to 22,053 all with par value of birr 1000(USD 125) per share. To this regard, in line to the current government policy the company has frothed its preparation to venture capital and so is looking for business partner, be it in the form of management contract or other modalities left to be negotiated in the interested parties besides, it should be noted that the aforementioned production capacities pertain on a single shift basis, and so could be increased launching additional shifts or removing the existing bottlenecks in the assembly line left to be identified by the world investor.

1.2.3 The Company's Main Product Lines are:

1. Military boots, civilian working boots, regular shoes including children and ladies' shoes, all in genuine leather for both local market and for export and

2. Glue (sole glue, vulcanizing glue, P.U. glue, and lasting glue) to local market and for own factory use.

The Company is specialized in vulcanizing molding process for soles that ensure sturdiness and lasting wear under the toughest condition. The Share Company has an annual capacity of producing 536,000 pairs of various shoes and 200,000 kg of multi purpose glue in 8 hours per day. The facility layout of the Share Company is arranged in two product lines: Civilian and military shoes product lines. The main process of the production systems are cutting, stitching, bottoming and finishing. These processes are explained very briefly here below.

Cutting: Cutting of leather to different shoe components is done by modern Hydraulic Cutting Machines.

Stitching: Assembling of the different components of the upper part of shoes is done by 104 different types of flatbed, post-bed, zigzag, Eyeleting Machines and so on

Lasting: Shaping the upper to the last is done by automatic counter molding machine, Toe, side and heel seat lasting machines, In addition to other lasting machines; it is equipped with a modern versatile type of lasting machine that lasts all types of civilian, children and ladies shoes.

Bottoming: Attaching lasted upper to the sole is done in two ways. The main bottoming line is direct vulcanization where the lasted upper and raw rubber is stacked on by using new modern p22 types of vulcanizing machines within 6 minutes. This new p22 type of vulcanizing machines can make two types of colors.

Unit Sole Attaching: This line is equipped with modern roughing, insole reinforcing, sole attaching, pressing and leveling machines.

Finishing: Trimming, polishing, shoe lacing and packing is done by different shoe finishing machines. In addition to the main processing line, there are also auxiliary lines.

Insole Preparation: Inside parts of shoe such as toe puff, counter, insole and stock lining are prepared by hydraulic cutting, insole forming, counter splitting and skiving, in sole trimming and so on.

Rubber Mixing: Raw rubber is mixed with other ingredients to give the desired output properties, with the help of three heavy roll calendars, two shaping and two cutting machines.

Unit sole Preparation: Different types of unit sole, tiles, sealing and so on are produced with the help of two press machines with four and three beds respectively.

Glue Manufacturing: The Shares Company produces four different types of glue, vulcanizing, sole, P.U. and lasing glue for the Share Company and commercial use.

1.2.4 Availability of raw materials

The company's major raw materials are processed leather, which is sourced from domestic tanneries. The country is among the ten endowed countries with cattle population.

1.2.5 Markets

The company is the only of its kind and all the heavy duty shoes processed are directly sold to government organizations like the ministry of defense and police forces as well and the public population at large. Referring to the past track records of the company, in the 1988's it used to Yemen and Uganda. It may as well have to look for the potential to export elsewhere.

The various types of glues are:

- Vulcanizing glue
- Sole glues
- Lasting glue
- P.u. glue. These glues are utilized by the factory and sold in the local market, which has a significant demand to it.

1.2.6 Manpower

The current number of permanent employees stands at 600 out of which 348 are men and the remaining are women. Most of the employees have acquired invaluable skills on account of that rich experience during their considerable years of service in the factory.

1.2.7 Facilities

Electrical power is obtained from the national grid of the Ethiopian Electric power corporation, while water requirements of the factory are met from the two deep well and municipality water supply.

1.2.8 The Existing Organizational Structure.

The existing organizational structure of the Company was implemented in the year 1998 E.C. According to this structure, the Company has three executive and seven functional organs.

The executive organs are-

1. The Authority of Public Enterprise
2. The Board of Directors and
3. The General Manager.

The functional organs are-

1. Administration Department,
2. Finance Department,
3. Commercial Department,
4. Production and Technical Department
5. Quality Control Service,
6. Market Research and Statistics Service &
7. Audit and inspection service,

1.3. Statement of the problem

In Ethiopia during the Dergue regime; since the government was following socialist ideology, state owned enterprises dominated overall sectors of the economy. However since 1991, the government of Ethiopia embarked up on privatization of state owned enterprises as an integral part economic reform program. Through this privatization program the government concentrates more on policy making and monitoring function; to enhance managerial efficiency, cost effectiveness and innovation in business activity; to decrease the budgetary burden of the state owned enterprises and to encourage local and foreign private investors. (Proclamation NO.146/1998)

According to Vernon and wortzel (1989) the financial and operating performance of the former state owned enterprises are important because developed and developing countries are not equally endowed with those factors likely to influence the success of privatization program. Indeed, the privatization efforts of most developing countries are inhibited by lack of the main ingredients for a successful privatization such as competent managers, entrepreneurs and investment capital.

So many researchers studied the impact of privatization up on the firm's financial and operating performance and they document positive and negative impact of privatization up on firm's performance.

For instance, (Boubakri and Cosset, 1998) review before-and after-performance of 79 privatized firms in 21 developing countries mostly middle income, including Bangladesh, Jamaica, Nigeria, Pakistan and Philippine and conclude that on average the firms in their sample indicated significant increases in profitability, operating efficiency, capital investment spending, output and employment, and a decline in leverage and an increase in dividends following privatization.

On the other hand Hakro and akram (2009) compare the operating and financial performance of firms before and after privatization in Pakistan. They document insignificant decline in profitability efficiency, output and dividends parameters.

The main purpose of this study is to evaluate the impact of privatization up on financial and operating performance of Tikur Abay Shoe Share Company and to provide justifications whether the firm`s financial prformance is detroriating or improving .

1.4 Objective of the study

1.4.1 General objective.

The general objective of the study is to investigate the impact of privatization up on financial and operating performance of Tikur Abay Shoe Share Company.

1.4.2 Specific objectives.

- To evaluate the profitability of the company.
- To Examine the operating efficiency of the company.
- To evaluate the capital investment.
- To assess the employment level of the company.
- To evaluate the leverage structure of the company.
- To assess the liquidity of the company.
- To assess factors that affects the financial and operating performance of TASSCo following privatization.

1.5 Hypothesis

Countries around the world have their own objectives in privatization programs and governments expect that privatized firms will increase their operating efficiency ,became profitable and increases their capital spending and became financially healthier; yet all governments fear these benefits will come at the economically (politically) painful cost of reduced employment in the privatized firms.

This paper has been tested the following hypothesis.

H1: There is an Improvement on TASSCo's profitability following privatization.

H0: There is no an Improvement on TASSCo's profitability following privatization

H1: There is an improvement on TASSCo's operating efficiency following privatization.

H0: There is no an improvement on TASSCo's operating efficiency following privatization

H1: There is an Increase on TASSCo's capital investment spending following privatization.

H0: There is no an Increase on TASSCo's capital investment spending following privatization.

H1: There is Decrease on TASSCo's employment level following privatization.

H0: There is no Decrease on TASSCo's employment level following privatization

H1: There is Decrease on TASSCo's leverage structure following privatization.

H0: There is no Decrease on TASSCo's leverage structure following privatization

H1: There is an Increase on TASSCo's liquidity position following privatization.

H0: There is no Increase on TASSCo's liquidity position following privatization.

1.6 Scope and limitations

Identifying and investigating all possible causes that affect the financial and operating performance of a company requires extensive research, much more time, sufficient information and energy. But this study is limited to some of them that currently affecting the TASSCo's operating performance. This study has been conducted on the evaluation of Financial and operating performance of Tikur Abay Shoe Share Company. The study covers three years pre privatization period(2003 to 2006,GC) and post five years (2007 to 2009,GC) of audited annual financial statements, using ratio analyses and T-test statistics, more concerned with trend analysis, which are the most important financial analyses in making business operations decisions. The company was not willing to give the audited financial statement of year 2009 so this has its own impact up on the result of the study.

The financial statement of year 2006 is excluded from the analysis because it includes both public and private ownership phase of the firm. The study also addressed some of the major causes that possibly affect the company's profitability and operating efficiency. In the evaluation process, independent valuation of attributes such as, inflation that could affect the financial performance of the company is not considered. Others like politics and economic cycle are not also the concern of this paper. In addition, the study was limited by financial and time constraints.

1.7 Significance of the study

This research has a varied area of contribution to Tikur Abay Shoe Share Company employees, management, and owners to know their current financial and operating performance and constraints that affect their performance following privatization. It also provides the base information for potential investors to take corrective actions regarding the investments in the industry. The study can serve as important insights for future researchers on evaluation of financial and operating performance related studies in the Industry. last but not least this study will help Ethiopian privatization agency to know the current position of the company.

1.8 organization of the paper

The organization of this study takes the following form: The paper is categorized in to five main chapters. Chapter one deals with introductory part which consists of background of the study, background of the company, statement of the research problem, objectives of the study, research methodology, significance of the study and scope and limitation of the study. The second chapter deals with literature review which have theoretical and empirical frame work. And the third chapter is about data and methodology. The fourth chapter is about data analysis and presentation. Finally, chapter four concludes the study and provides relevant recommendation.

Chapter II: Literature Review

2.1 Review of Theoretical Literature

Several developing and transition economies have embarked on extensive privatization programmers in the last one and a half decades or so, as a means of fostering economic growth, attaining macroeconomic stability, and reducing public sector borrowing requirements arising from corruption, subsidies and subventions to unprofitable SOEs. By the end of 1996, all but five countries in Africa had divested some public enterprises within the framework of macroeconomic reform and liberalization (White and Bhatia, 1998).

The recent history of privatization begins in the early 1980s when the Thatcher government in the United Kingdom started to privatize state-owned enterprises (SOEs) on a wide scale. After the collapse of the Communist political system in the late 1980s, many transition economies also launched comprehensive privatization programs. Nowadays, privatization is a worldwide phenomenon that forms an important element of the increasing use of markets to allocate resources.

Although privatization seems to be accepted as a useful method to restructure the economy, it is still not clear under which conditions privatization is successful, and how exactly it affects the firm behavior and macro-economic performance of a country. Some studies point at success stories (especially in non-transition economies); while others argue that there are major failures, such as the privatization program in Russia (Megginson and Netter, 2001, and Parker and Kirkpatrick, 2005). It is therefore no surprise that a lively debate is taking place on the effectiveness of privatization. This debate focuses on a long list of issues, such as the optimal preconditions of privatization, under pricing of initial public offerings (IPOs), the most appropriate form of privatization, the effects of privatization on firm performance and

employment, the impact of the economic environment – and especially measures other than privatization (such as price deregulation) – on the effectiveness of privatization, the interrelationship between corporate governance and privatization, and the impact of privatization on the development of the domestic financial system, especially with regard to the stock market.

2.2 Privatization in Developing Countries:

In the realm of public policy, one of the most unprecedented global features in the last quarter of the twentieth century has been privatization. During the past two decades, governments all over the world introduced various forms of privatization irrespective of their economic contexts, political orientations, and ideological positions. This current trend represents almost a reversal of the traditional postwar policy orientation based on the assumptions of welfare state, planned development, and public-sector-led economic growth, which became entrenched in both developed and developing nations during the period between the 1950s and 1970s (Esman, 1991).

In developing nations such as Taiwan, South Korea, Singapore, Malaysia, Thailand, Indonesia, Brazil, and Mexico, beyond the conducive external factors such as foreign aid, foreign market, and foreign investment, the state sector played a crucial role in accelerating socioeconomic development (Leipziger and Thomas, 1993).

However, this tradition of state-led policies, programs, and performance came under challenge posed by various critical issues—especially the growing dissatisfaction among citizens with bureaucratic inefficiencies, the diminishing performance of public enterprises, the declining public confidence in government institutions, the deteriorating situation of inflation allegedly caused by public sectors deficits, the rise of neoliberal critique of state intervention, and the advocacy for market-driven remedies, and so on (Clarke, 1994)

This challenge to the established state-centered policy perspective was reinforced further by the collapse of major socialist states and the worldwide triumph of market ideology (Hague, 1999).

2.3 Methods and objectives of privatization

2.3.1 Objectives

Public ownership and nationalized companies have many economic ills. Thus privatization attracts extensive objectives. Privatization program has far-reaching goals, which may have as much to do with demonstrating a shift in ideology as improvement in micro level efficiency and strategic planning. However (Kate 2001) has stated that the following are the main objectives of most privatization programs:

- Improving the efficiency of the enterprise
- Increase competition
- Improve the government fiscal position
- Develop the private sector
- Broaden the distribution of ownership and
- Reduce political interfaces

In general privatization is associated with the unleashing private capital and entrepreneurship from the restrictions imposed by excessive government presence and political interference in the economy (Kate, 2001).

According to the World Bank, the main tenet of privatization is that of enhancing efficiency rather than maximizing short- term government revenues (kikeri, et al 1992).

Kekeri (1992) also argues that privatization when correctly conceived and implemented, fosters efficiency, encourage investment, brings new growth and employments and free public resources and infrastructure and social programs. Privatization of the economy and restructuring of the monetary and fiscal systems are mutually supportive objectives; privet ownership of the large portion of the fiscal system appears essential to its appropriate functioning, while the reorganization of banking and financial enterprises appears a necessary condition for the privatization process to be effectively sustained.

In addition, privatization is associated with institutional changes which can be summarized in to three main points. First a clear distinction between ownership, enterprise and labor is introduced. Second, the firm is introduced to operate in direction of individual profit. Third, a competitive environment is created by lifting barriers to entry and encouraging completion (kikeri, et al 1992).

2.3.2 Methods of privatization

Broadly, there are two aspects: privatization of management and privatization of ownership. The distinction is not always clear- cut, as there are almost endless variations. Privatization of management includes management contracts, lease or concessions. It may be more appropriate in low-income countries with weak capital markets and banking institutions. Leasing and management contract can be less potentially contentious than outright sales. Privatization of ownership is a conversion of enterprises formally owned by the government in to private ownership.

Possible modalities

- Voucher /mass privatization –non-sale distribution
- Initial public offer/IPO
- Competitive tender for shares and share auction
- Negation sales of shares/assets
- Asset sale
- Joint venture
- Lease
- Management contract etc.

2.4 World Bank policy towards privatization.

The World Bank has keenly supported privatization in Africa. By the end of 1995, all but six (out of forty-eight) African countries had divested some public enterprise and all but eleven had had some World Bank lending in support of the policy. Cambeli-white o., a .Bhatia (1998)

However, the core mandate of the WB is to eradicate poverty. Privatization, as a central policy promoted by the WB, must therefore somehow be expected to contribute to this overall goal.

Privatization is promoted because of the perceived weaknesses of public ownership and poor track record when it comes to enterprise reform. The WB takes a strong stance on privatization as opposed to enterprise reform because efforts at reform which stopped short of privatization are regarded as unsuccessful (kikeri, S.1992).

"Few governments have been able to introduce–and keep in place–the large number of complex and demanding measures needed for effective public enterprise reforms."

The problems which have emerged under state ownership are spelt out (and to some extent related to poverty): "The costs have been high. In many countries, inefficient but privileged public enterprises drained budgets, diverted resources from health and education, seriously damaged the health of the banking sector, and created obstacles for the development of the private sector. Observing the immense difficulties of reforming public enterprises without changing ownership, the Bank emphasizes divestiture as a means of locking in the gains from reforms."

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Pointers are provided as to how privatization can be carried out: Governments “must: a) devise sect oral policies that introduce and maintain competition; b) establish and maintain a sound regulatory framework for the remaining monopolies, public and private; c) maintain transparency in transactions and convince investors that their investments are secure; d) negotiate, monitor, and enforce contracts with private suppliers of management and financing; e) ensure that resources from privatization sales are put to productive uses and f) manage the inevitable political and social tensions that arise as enterprise reforms are implemented, especially the critical issues of foreign ownership and labor layoffs. With scarce capacity for governance, a constant theme of WB literature, it might be thought that governments have their work cut out for them dealing with all the issues that accompany privatization.

2.5 Privatization and Efficiency Gains: Theories and Evidences.

Several theories have been put forward to predict and explain why we would expect some Productive (internal) efficiency gain as a result of privatizing public entities (Vickers and Yarrow, 1988). Among them, the property right theory is perhaps the most influential. The theory relies heavily on the notion that once privatized there will be a greater incentive for managers (who are agents to shareholders) to minimize cost due to the discipline force of corporate takeovers, the threat of bankruptcy and greater shareholders' monitoring. Inefficient managers in a private entity created incentive for corporate takeovers from outside parties since there is a surplus to be gained through better management. Bankruptcy threat is also either non-existent or weak for public firms. This is certainly not the case for private firms. In addition, arguments can also be made that private shareholders are keener at monitoring managerial efforts and performances than public officials or politicians. De Alessi (1980) in explaining the poor monitoring of public firms’ performance stated that: "The crucial difference between private and political (publicly owned) firms is that ownership in the latter effectively is non-transferable. Since, this rules out specialization in their ownership, it inhibits the capitalization of future consequences into current transfer prices and reduces owner’s incentives to monitor managerial behavior."

However, there are other theories demonstrating that shareholders' monitoring are no greater(Vickers and Yarrow, 1988) and the threat of takeover is rather weak (Grossman and Hart,1980) for private firms. Even though ownership of public firms is not transferable in theory, politicians who fail to do a good job of monitoring public performance can be voted out of office. In addition, financial surplus created by a well- monitored public firm can be used to confer benefits to at least some voters thus enhancing the chance of the electoral success of the politicians concerned. Both forces tend to encourage greater monitoring of public firms.

The Grossman and Hart's argument relies on the idea that shareholders may free ride on the effort of the party involved in mounting a takeover. The threat of takeover is weaken because if shareholders know that there is a pending takeover then they might as well hold on to their shares because there will surely be some surplus to be created after takeover (otherwise why is there a takeover in the first place). This free riding behavior actually hinders takeover and hence protects inefficient managers.

2.6 Privatization in Ethiopia

Privatization in Ethiopia is carried out as a part of economic stabilization programs advocated by IMF and the World Bank. A subsidy public enterprise was lifted in1992 when the economic reform and rehabilitation program was launched. besides microeconomic liberalization were under taken, investment and labor law has revised, prices where decontrolled, with the exception of few of basic commodities, transport tariff was deregulated and zone fleet administration abolished(eshete, 1994). Proclamation No. 87/1994 and 1998 established the Ethiopian privatization agency (EPA) in February of 1994. Since then EPA has became the lead agency in carrying out the process of privatization of public enterprises. In addition to the powers and duties mentioned. EPA has a power to investigate and decide on claims of ownership in respect of property taken in violations of the relevant proclamations, in accordance with proclamation No. 193/2000. The agency is accountable to the ministry of trade and industry and administered by a board of directors and managed by a general manager.

The objective of Ethiopian privatization agency as per proclamation No.146/1998 are to generate revenue required for financing development activities undertaken by the government; change the role and participation of the government in the economy by enabling it to exert more effort on activities requiring its attention; and promote the country's economic development through encouraging the expansion of the privet sector.

Since Ethiopia embarked on the road to liberalization and a market economy in the 1991EC, the privatization of state-owned enterprises has became an important element of the nation wide reform program. All the activities under taken by Ethiopian privatization agency are therefore part and parcel of the reform measures. They are well integrating in to a large political, social and economic framework of Ethiopia with in historical context.

EPA started to implement program first by privatizing small retail trade outlets and hotels as well as small-scale manufacturing and agro-processing enterprises .the reason was to gain first hand experience, which could be used in inviting prospective investors to participate in bids for enterprises floating for privatization.

2.6.1 Privatization objectives and strategies of Ethiopia

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:

a) Maximizing revenue and ensure a better ownership – the private sector

b) Relieving tied resources and re-deploy into other areas of higher priority.

c) Create a dynamic and new industrial entrepreneur group that will be a capable ally and partner in development.

d) 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 programs 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. For example, as shown in the table 1 below, the privatization program objectives of Ethiopia have similarities as compared with other neighboring African 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.

Table 2.1 privatization program objectives in some African countries

Country	objectives
Ethiopia	• Maximize revenue • Relieve tied resources • Private sector development • Attract investment
Malawi	•Reduce fiscal drain • Increase efficiency • Increased competition • Public participation
Tanzania	• Improved enterprise efficiency • Reduce fiscal drain • Wider ownership and management • Mobilization of domestic and foreign capital
Zimbabwe	• Raise revenue • Reduce budget deficit • Change government role • Let parastatals make their own decisions and move away from bureaucracy • Make parastatals operate mare viably/improve efficiency
Kenya	• Reduce budgetary drain • Broadening ownership base
Uganda	• Reduce fiscal drain • Raising Revenue • Promotion of local private sector

Source: Adopted from Price Waterhouse Pan African Consultants, 1998.

2.6.2 Privatization modalities in Ethiopia

Privatization is basically the transfer of government assets or shares to the private sector. A different person defines privatization in slightly different way. The definition ranges from actual ownership title transfer to delegation of operational control to the privet sectors.

A transaction is recognizing as privatization if it only takes place with a private entity. A transfer to another public enterprise is not normally considered as privatization. Privatization can be achieved through a number of transaction involving money or not(vouchers) .these transaction are called **modalities** which in simple word means method of privatization.

Selections of modalities depend on the characteristics of the enterprise as well as the objective of the government. Some enterprises may have identifiable needs investment, management, marketing, etc.) Others can be managed by anybody. The government may want to spread ownership, empower local investors, go out of operation while retaining ownership, etc .there are a dozen of modalities to date. Until the end of 1996 over 18 deferent modalities were used in Africa alone. To date, Ethiopia has used a few modalities namely:

1, asset sale: retail outlets, hotels and restaurants, manufacturing and mining enterprises.

2, lease /sales: adiey ababa yarn and dire dawa textile

4, joint venture with strategic investors: tobacco,

5, management contract: awassa, combolcha textiles.

6, competitive sales of shares: beverage sector, awassa flour

Source :(privatization review published by the Ethiopian privatization agency, February, 2001)

2.6.4 Pre-privatization

The privatization preparation and planning department performs all preliminary work and studies to prepare an enterprise for selling. Its duties to make enterprise ready for privatization include: preparing sequence and priority plans for the privatization, collecting necessary data from the

enterprises to be privatized. The data include fixed asset ,financial statuses, technical, employment, performance, etc conducting studies and analysis of the enterprise to come up with sound options of privatization ,value the assets and business of the enterprise to be privatized and act as counterpart for external consultant in case where external consultants do valuation and others studies.

The department process stock data from public enterprises, restitution cases approved by the restitution department of the EPA, and reports by consultants, to produce assets and valuation Reports and Privatization strategic plans.

When the privatization preparation and planning department has completed all the necessary work to make an enterprise ready for sale ,the implementation departments takes over the final selling of an enterprise this department prepares bid document advertise the bid and monitors the implementation of the privatization process until a forma handover of the enterprise to the buyer takes place.

Following signing of an agreement, a legal transfer of enterprise from the government to the buyer takes place depending on the mode of divestiture. The transfer also includes the physical handover of assets to the new owner. Share transfer may also be done as per the contract signed.

Source: EPA, 2002

2.6.5 Privatization implementation

The actual process of privatization is handled by the implementation department of the EPA which is entrusted with the following obligation: preparation of bid documents, advertising and selling bids, preparation of contract agreements, monitoring the transfer of the enterprise, reporting differences in the balance sheets, i.e. between the previously worked out valuation and the actual value at the time of the transfer, reporting the concern to the concerning organs and publishing information memorandu**m.**

In overseeing the formal handling-over of an enterprise, the department produces tender documents, transfer report, payment monitoring reports, and performance report based on

valuation reports , enterprise profile , restitution cases, payment data, and buyer information. Source: EPA, 2002

2.6.6 Post- privatization

The post privatization department is responsible for dealing with monitoring issues after an enterprise have been privatized. the responsibilities of the department include: monitoring whether or not the investors are fulfilling their commitments, following up and ensuring that the sellers obligation are met, and collecting data on enterprises privatized. The department maintains links with privatized institutions to carry out its various activities once it takes over the privatization process from the implementation department. Source: EPA, 2002

2.7 Basic tools of financial analysis

Financial analysis is the process of identifying the financial strength and weakness of the firm by properly establishing relationships between the items of the balance sheets and profit and loss account. Foster (1986) concludes that financial ratios are measures that show a proportional relationship between two factors, such as sales compared to working capital or liabilities compared to net worth. Often they are used to judge the investment suitability of a particular company; a firm's ratios can be compared to its own past performance and/or to the performance of the industry as a whole. Financial ratios are calculated from the figures given in the firm's annual financial statement. Financial ratios can be designed to measure any aspects of the performance of the company. In general financial analysts use the ratios as one tool in identifying the areas of strength and weakness in the firms.

To evaluate the Tikur Abay Shoe Share Company, time series analysis had been used in this paper. Anthony (1975) defines time series analysis or trend analysis as the process of comparing the company's present ratio with the past ratios. It gives an indication of the direction of changes and reflects whether the firm's financial performance has improved, deteriorated or remain constant over time. The analyst should not simply determine the changes, but, more importantly, he/she should understand why ratios have changed.

There are several types of ratios: profitability or operating ratios which measure the success of a company's operating performance; activity or efficiency ratios which indicate how effectively a company uses and controls its assets (Foster, 1986). liquidity ratios which measure a firm's ability to meet its short-term financial obligations; leverage ratios which measure ability to meet long-term obligations; The following discussions briefly presents the salient features of profitability ,liquidity, leverage, and activity ratios.

2.7.1 Profitability ratios:

Profitability is a relative term. It is hard to say what percentage of profits represents a profitable firm, as profits depend on such factors as the position of the company and its products on the competitive life cycle (for example profits will be lower in the initial years when investment is high), on competitive conditions in the industry, and on borrowing costs.

For decision-making, it is concerned only with the present value of expected future profits. Past or current profits are important only as they help to identify likely future profits, by identifying historical and forecasted trends of profits and sales. Profitability ratios measure operating efficiency and ability to ensure adequate return to shareholders. In other words, they are used to evaluate the overall management effectiveness and efficiency in generating profit on sales, total assets and owners' equity. The profitability ratio helps to know whether profits are generally on the rise; whether sales stable or rising; how the profits compare to the industry average; whether the market share of the company is rising, stable or falling; and other things that indicate the likely future profitability of the firm. Profitability ratios help to measure how well a company is managing its expenses. These measurements allow evaluating the company's profits with respect to a given level of sales, a certain level of assets, or the owner's investment. It is related to the effectiveness with which management has employed both the total assets and the net assets as recorded on the balance sheet. These ratios are usually created by relating net profit, defined in a variety of ways, to the resources utilized in generating that profit.

Source: http://www.investopidia.com

The researcher used three ratios so as to measure the profitability of the company namely: return on sales (ROS), return on asset (ROA), and return on equity (ROE).

2.7.1.1 Return on sales (ROS)

A ratio widely used to evaluate a company's operational efficiency. ROS is also known as a firm's "operating profit margin". It is calculated using this formula:

$$= \frac{\text{Net Income (Before Interest and Tax)}}{\text{Sales}}$$

This measure is helpful to management, providing insight into how much profit is being produced per dollar of sales. As with many ratios, it is best to compare a company's ROS over time to look for trends, and compare it to other companies in the industry. An increasing ROS indicates the company is growing more efficient, while a decreasing ROS could signal looming financial troubles. Source: http://www.investopidia.com

2.7.1.2 Return on Assets (ROA):

ROA Measures the overall effectiveness of management in generating profits with its available assets. A company is efficient if it can generate an adequate return while using the minimum amount of assets. Efficiently working company does not require too much cash for everyday operations and can shift its excesses to investments in new spheres.

Consequently, the ROA is considered a critical ratio for determining a company’s overall level of operating efficiency and it shows how much profit was earned on the total capital used to make that profit. Here, the profitability ratio is measured in terms of the relationship between net profits and assets. The ROA may also be called profit-to-asset ratio. The formula is as follows:

$$\text{Return on assets} = \frac{\text{Net profits}}{\text{Total assets}}$$

Source: http://www.investopidia.com

2.7.1.3 Return on Equity (ROE):

It is another very important measure of a company's profitability that reveals how much profit it generates with the money shareholders have invested. The return on equity measures the return earned on the owners' capital (both preferred and common stockholders') as an indicator of management's performance.

High return on equity indicates effective management performance but low return on equity indicates ineffective management performance.

$$\text{Return on Equity} = \frac{\text{Net income}}{\text{Shareholders' Equity}}$$

Source: http://www.investopidia.com

2.7.2 Liquidity Ratios:

The liquidity of a firm is measured by its ability to satisfy its short-term obligations as they come due (Gitman, 2004). Liquidity also stands for ability of a company to convert its assets into cash quickly and with lower costs as possible. Such liquid assets are necessary to cover any "financial emergencies" and play as a buffer in company's operations. Liquidity ratios reflect the short-term financial strength/solvency of a company.

The liquidity of a business firm is usually of particular interest to its short-term creditors since the liquidity of the firm measures its ability to pay those creditors.

Several financial ratios measure the liquidity of the firm. Those ratios are the current ratio, the quick ratio or acid test, cash ratio and net working capital.

2.7.2.1 Current Ratio: The current ratio, one of the most commonly cited financial ratios, measures the company's ability to meet its short-term obligations by using only current assets. The current assets consist of cash and assets that can easily be turned into cash and the current liabilities consist of payments that a company expects to make in the near future. Thus, the ratio of the current assets to the current liabilities measures the margin of liquidity. It is known as the current ratio. The current ratio is probably the best known and most often used of the liquidity ratios.

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

A satisfactory current ratio would enable a company to meet its obligations even when the value of the current assets declines. The higher the current ratio, the larger is the amount of birr available per birr of current liability, the more is the company's ability to meet current obligations and the greater is the safety of funds of short-term creditors. Thus, current ratio, in a way, is a measure of margin of safety to the creditors. http://www.wise geek.com

2.7.4 Leverage ratios:

Financial leverage ratios are also called debt ratios. You may also find them called long-term solvency ratios. They measure the ability of the company to meet its long term debt obligations, such as interest payments on debt, the final principal payment on debt, and any other fixed obligations like lease payments.

These debt ratios allow the management of the company to determine how well the business can meet its long-term debt obligations. These ratios are worth nothing, or very little, in isolation. You e to pay its debt, it will be forced into bankruptcy. On the positive side, use of debt is beneficial as it provides tax benefits to the firm, and allows it to exploit business opportunities and grow. Total debt includes short-term debt (bank advances + the current portion of long-term debt) and long-term debt (bonds, leases, notes payable).have to be able to do trend and industry analysis in order to be able to determine how well you are managing your debt position.

"When a company borrows money, it agrees to make a series of fixed payments in the future. Because their shareholders get only what is left after the debt holders have been paid, the debt is said to create financial leverage. In extreme cases, if crisis times come, a company may be unable to pay its debts" (Brealey, 2003). Financial leverage enables a company to have an asset base larger than its equity. A company can finance its assets with equity or with debt.

Usual practice is expanding the equity through borrowings and the creation of other liabilities like accounts payable, accrued liabilities, and deferred taxes. Financial leverage increases the company's ROE as long as the cost of the liabilities is less than the return from investing these funds. "While a company's shareholders can potentially benefit from financial leverage, it can also increase their risk" (Palepu, 2006).

Debt ratios show the extent to which a firm is relying on debt to finance its investments and operations, and how well it can manage the debt obligation, i.e. repayment of principal and periodic interest.

2.7.4.1 Total Debt to Assets Ratio:

This component ratio is also-called "Debt Ratio" and measures the proportion of total assets financed by company's creditors. This ratio reflects the relative claims of creditors and shareholders against the assets of the company. Alternatively, this ratio indicates the relative proportions of debt and equity in financing the assets of the company. The Debt Ratio tells the percent of funds provided by creditors and to what extent the company's assets protect creditors. The higher the debt ratio, the greater the amount of other people's money being used in an attempt to generate profit and the higher the financial cost and restrictions from creditors

The ratio is calculated as follows: $\text{Debt ratio} = \dfrac{\text{Total liabilities}}{\text{Total assets}}$

Creditors prefer moderate or low debt asset ratio because the lower the ratio the greater the caution of liquidation. That is, low or moderate debt asset ratio provides creditors more protection in case a company experiences financial problems.

The higher Total Debt to Assets Ratio, the greater degree of indebtedness and the more financial leverage a company has. . A low Debt Ratio would indicate that the company has sufficient assets to cover the debt load. Creditors and management favor a low Debt Ratio.

2.8 Empirical literatures

From an empirical standpoint, the phenomenal increase in the number of privatization programmers in both developed and developing economies has generated a lot of research interest. Many researchers around the world studied the impact of privatization on financial and operating performance of privatized firms in developing and developed countries.

Juliet D'Souza and William L. Megginson(1999) compared the pre- and post-privatization financial and operating performance of 85 companies from 28 industrialized countries that are privatized through public share offerings between 1990 and 1996. They document significant increases in profitability, output, operating efficiency and dividend payments--and significant decreases in leverage ratios--for their full sample of firms after privatization, and for most subsamples examined. Capital expenditures increase significantly in absolute terms, but not relative to sales. Employment declines, but insignificantly. Combined with results from two previous, directly-comparable studies, these findings strongly suggest that privatization yields significant performance improvements.

Narjess Boubakri and Jean-Claude Cosset (1998) they examines the change in financial and operating performance of 79 companies from 21 developing countries that experience full or partial privatization over the period 1980 to 1992. To take account of the possibility that some of the differences between pre privatization and post privatization performance could be due to economy wide factors. They use performance measures adjusted for market effects in addition to unadjusted performance measures. For both unadjusted and market-adjusted performance measures, they document significant increases in profitability, operating efficiency, capital investment spending, output (adjusted for inflation), total employment and dividends. They also find a decline in leverage following privatization but this change is significant only for unadjusted leverage ratios. Additionally, their results are generally robust when they partition their data into various sub samples. However, the evidence suggests that privatization yields

greater benefits for companies operating in developing countries with high income per capita and for companies whose governments surrender voting control.

Omran (2001) Evaluates the financial and operating performance of newly privatized Egyptian 69 firms, which have been privatized from 1994-1998. He documents significant improvement in profitability, operating efficiency and capital expenditure, dividends and liquidity and significant decrease in employment, leverage and risk, where as output showed an insignificant decrease.

Martin and Parker (1997) assess the impact of privatization on 11 major firms privatized in the UK in the 1980s, they document; Significant improvement in profitability, operating efficiency and capital expenditure, dividends and liquidity. And significant decrease in employment, leverage and risk, where as output showed an insignificant

The other researcher is **Osman (2009);** he studied the financial performance of 16 privatized firms in Sudan during the period 1990-2002.and he document Statically insignificant improvement in the financial performance of the privatized enterprises after privatization, except for real sales per employee.

Hakro and akram(2009). They compare the operating and financial performance of firms before and after privatization in Pakistan. And they document insignificant decline in profitability efficiency, output and dividends parameters.

Jerome (2006) examined the financial and operating performance of three newly privatized enterprises in competitive sector in Nigeria by comparing the pre and post privatization performance. And measure the change in any given indicators of performance by comparing its average value of five years before and five years after privatization. And they document Significance increase on profitability, productive efficiency, employment, capital investment, output prices and taxes, increase in technical efficiency.

And finally **Engelbert et.al (2005)** Measures the operating performance of Austrian firms that were privatized during the period of 1985-1995. They used Wilcox on signed rank test, test statistic z and (binomial) proportion test and document No significant difference between state ownership and privatization.

The following table shows summary of different empirical studies.

Table 2.2 .Summary of empirical studies

Researcher	Sample description and study period.	Methodology	Empirical finding
D'Souza and megginson(1999)	Compare the pre and post privatization financial and operating performance of 85 companies from 18 developing 13 industrialized countries that experienced full or partial privatization through public share offerings during the period 1990 to 1996.	Test for the significance of median changes in ratio values in post versus pre privatization period. And binomial test for percentage of firms changing as predicted. And they considered -3_-1 to +1_ +3 years for comparison.	Significant increase in profitability, real sales, operating efficiency and dividend payments and significant decrease in leverage ratios. Capital investment spending and employment levels declined, but changes were not statistically significant.
Martin and Parker (1997)	assess the impact of privatization on 11 major firms privatized in the UK in the 1980s,	Wilcox on signed rank test, test statistic z and (binomial) proportion test.	Significant improvement in profitability, operating efficiency and capital expenditure, dividends and liquidity. And significant decrease in employment, leverage and risk, where as output showed an insignificant decrease.
Jerome (2006)	Examined the financial and operating performance of three newly privatized enterprises in competitive sector in Nigeria by comparing the pre and post privatization performance.	Measured the change in any given indicator of performance by comparing its average value of five years before and five years	Significance increase on profitability, productive efficiency, employment, capital investment, output

		after privatization.	prices and taxes increase in technical efficiency.
Omran(2001)	Evaluation of financial and operating performance of newly privatized Egyptian 69 firms, which have been privatized from 1994-1998.	Wilcox on signed rank test, test statistic z and (binomial) proportion test.	Significant improvement in profitability, operating efficiency and capital expenditure, dividends and liquidity. And significant decrease in employment, leverage and risk, where as output showed an insignificant decrease.
Boubakri and cosset (1998)	Compared three years average pre and post privatization financial and operating performance ratio to the three years pre privatization for 79 companies from 21 developing countries that experience full or partial privatization over the period 1980 to 1992.	Test for the significance of median changes in ratio values in post versus pre privatization period. And binomial test for percentage of firms changing as predicted.	Significant increase in profitability, operating efficiency, capital investment spending / output, total employment, dividend and decline in leverage.
Osman (2009)	Studied the financial performance of 16 privatized firms in Sudan during the period 1990-2002.	Wilcox on signed rank test, test statistic z and (binomial) proportion test.	Statically insignificant improvement in the financial performance of the privatized enterprises after privatization, except for real sales per employee.
Hakro and	Compare the operating and financial performance of firms before and after privatization in Pakistan.	Wilcox on rank test(z-test)	They document insignificant decline in profitability efficiency, output

akram(2009)			and dividends parameters.
Engelbert et.al(2005)	Measures the operating performance of Austrian firms that were privatized during the period of 1985-1995.	Wilcox on signed rank test, test statistic z and (binomial) proportion test.	No significant difference between state ownership and privatization.

Chapter III: Data Source and Methodology

3.1.1 Study Design

The main objective of this study is to evaluate the financial and operating performance of Tikur Abay Shoe Share Company.

The study is both descriptive and quantitative type. The company was privatized in 2006G.C.so that the researcher will consider the latest pre and post privatization annual reports (from year -3 to year +3). These six consecutive years will help to have a clear picture of the company's financial and operating performance before and after privatization.

To achieve the objectives set in the study required thorough explanation of all operations that has been done according to methodology of the study. It is important that methodology of financial analysis that will be used here has been especially adapted for needs of the study (in a way of selection of methods that will "work" with particular financial statements). The study approach will include use of different techniques devoted to their specific needs and aims. The analysis will include studying of common size statements analysis and financial ratio analysis.

3.1.2 Sight selection and description.

Tikur Abay Shoe Share Company is one of the biggest and earliest shoe manufacturing enterprises in the country. It is located 10KM far from center of Addis Ababa (the capital of Ethiopia). It has been in the business for the last 56 years and it was privatized by five share holders in the year 2006. While selecting TASSCO as a case study; size and age of the company was taken in to consideration because the company is the biggest shoe industry in the country.

3.1.3 Data Collection Methods and Tools

The data used for this study was predominantly secondary data .The secondary data was collected from the annual financial statements of the company .In order to support the secondary data, additional information's was obtained by primary data gathering tool through conducting unstructured interview and focus group discussion especially to identify possible causes that affect the financial and operating performance the company.

The interview was conducted with selected officials of the company. Judgmental sampling was used to select the interviewees. This judgmental sampling is taken based on who provided the best information for the purpose of this study.

3.1.3 Data analysis

Data analysis part contains study of financial statements like the balance sheet and income statement. The data that was collected through the above tools was analyzed using the techniques of ratio analysis and t-test statistics to compare the financial and operating performance trend before and after privatization. T-test statistic particularly helps to calculate the mean values of the each variable before and after privatization, mean changes due to privatization, t-values and significant level. The analyzed information's are presented by using graphs and tables that are appropriate to explain the facts. Ten financial performance indicators are calculated as average of three years before and three years after privatization .under profitability three ratios (return on sales, return on asset and return on equity),under operating efficiency (sales efficiency and net income efficiency) ,under capital investment(capital expenditure/ total asset and capital expenditure / total sales), employment(total NO. of employee), under leverage(total debt/total asset) and finally under liquidity (current asset/current liability) were considered. The following table shows the major ratios, proxies (performance indicators) and predicted relationships.

Table 3.1 Characteristics, proxies and predicted relationships.

Characteristics	**PROXIES(** Performance indicators)	Predicted relation ships Subscripts: A: after B: before
Profitability	Return on sales(ROS) = Net Income / Sales Return on assets(ROA)) = net Income / Total Assets Return on equity(ROE)) = Net Income / Total Equity	**$ROS_A > ROS_B$** **$ROA_A > ROA_B$** **$ROE_A > ROE_B$**
Operating efficiency	Sales Efficiency (SALEFF) = Sales / Total Employment NI Efficiency(NIEFF) net income /Employment	**$SALEFF_A > SALEFF_B$** **$NIEFF_A > NIEFF_B$**
Capital investment	Capital Expenditure to Sales (CETS) Capital Expenditure to asset(CETA)	**$CETA_A > CETA_B$**
Employment	Total Employment (EMPL) = Total Number of employees	**$EMPL_A < EMPL_B$**
Leverage	Debt to Assets (TDTA) = Total Debt / Total Assets	**$TDTA_A < TDTA_B$**
Liquidity	Current ratio Current asset to current debt	$LIQ_A > LIQ_B$

Chapter IV: Results and Discussions.

4. Empirical results

The analysis conducted in this section compares the pre- privatization and post privatization operating and financial performance of Tikur Abay Shoe Share Company. This paper was done on the impact of privatization up on the financial and operating performance of Tikur Abay Shoe Share Company over the period 2003 through 2009. The research conceder's pre and post privatization data's so as to detect or investigate the possible changes that are observed following privatization as per the expectation of the government (objective of privatization).

The Government expect that privatized firms will increase their capital spending, and became financially healthier; yet all governments fear these benefits will come at the economically and/or politically cost of reduced employment in the privatized firms. Specifically this paper tests the hypothesis that privatization increases the firms profitability, increases its operating efficiency, decreases employment and decreases leverage. The testable predictions and empirical proxies indicated in chapter one was employed and all ratios were calculated for six years i.e. 3 years before and 3 years after privatization.

To test these predictions, in this study first empirical proxies for the company are computed over the pre- and post privatization period (pre privatization years 2003 through 2005 and post privatization years 2007 through 2009). Since the year of privatization year 2006 includes both public and private ownership phases. So that it is excluded from the analysis. The researcher uses financial data's like balance sheet, profit and loss account, statement of owner's equity etc. and calculate different financial ratio's before and after privatization.

The results were reported on the basis of descriptive statistics and using t-test statistics so as to compare the mean values of variables before and after privatization. Then the researcher point out the possible causes that are supposed to affect the financial and operating performance of the company.

4.1 Profitability change.

Profitability is the most important indicator to measure the performance of firms. As a firm moves from public to privet ownership its profitability should increases. Privatization typically transfers control rights and cash flow right to the managers who then show the greater interest in the profit and efficiency than did the politicians (boycko et al. (1996)). But the results of this study shows that all profitability ratios measured by return on sales (net income to sales) , return on asset(net income to asset) and return on equity (net income to equity) ratios doesn't show any improvement as expected in case of Tikur Abay Shoe Share Company rather mean value of the three ratios shows decline. This result is surprising. The literature provides persuasive evidence of profitability improvements following privatization elsewhere (Megginson, Nash, and Randenborgh (1994), Boubakri and Cosset (1998), and D'Souza and Megginson (1999), for example). But there is a general trend toward declining profitability in case of Tikur Abay Shoe Share Company even though the decline is statistically insignificantly.

4.1.1. Return on sales (ROS)

This measure is helpful to management, providing insight into how much profit is being produced per dollar of sales. As with many ratios, it is best to compare a company's ROS over time to look for trends, and compare it to other companies in the industry. An increasing ROS indicates the company is growing more efficient, while a decreasing ROS could signal looming financial troubles. ROS trend in TASSCo shows decline following privatization.

The following table shows the mean values (before and after privatization), mean change due to privatization, t-value and significant level of return on sales of Tikur Abay Shoe Share Company

Table 4.1, Performance Indicator: ROS

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	significance	comment
Return on sales(ROS)	0.0190	0.0483	-0.02933	-1.554	0.260	*insignificant

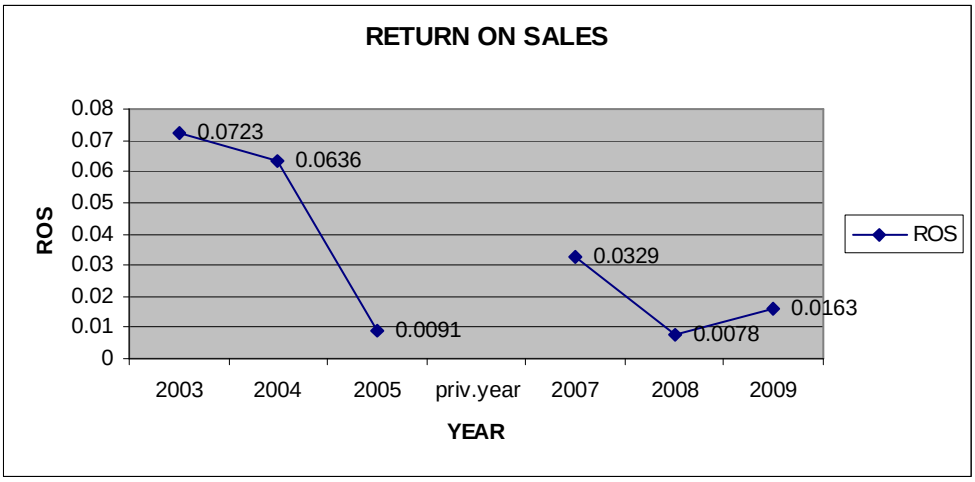
Source: SPSS output.

* **At 5 % significant level**

The above table reveals that; the mean value of ROS decline from 0.0483 before privatization to 0.0190 after privatization. The decline is statistically insignificant at 5% significant level and this indicates that the company profit per dollar of sales declines following privatization. The result is contrary to the expectation of the government and privatization objective because government expects significant increment in ROS following privatization.

The return on sales trend of the company before and after privatization will be displayed bellow by using line chart.

Fig 1, return on sales trend.



Source: **financial statement of TASSCo.**

4.1.2 Return on asset (ROA)

An indicator of how profitable a company is relative to its total assets. ROA gives an idea as to how efficient management is at using its assets to generate earnings. Calculated by dividing a company's annual earnings by its total assets,

ROA tells you what earnings were generated from invested capital (assets). ROA for public companies can vary substantially and will be highly dependent on the industry. This is why when using ROA as a comparative measure, it is best to compare it against a company's previous ROA numbers or the ROA of a similar company.

The following table shows the mean values of ROA (before and after privatization), mean change due to privatization, t-value and significant level.

Table 4.2., Performance Indicator: ROA

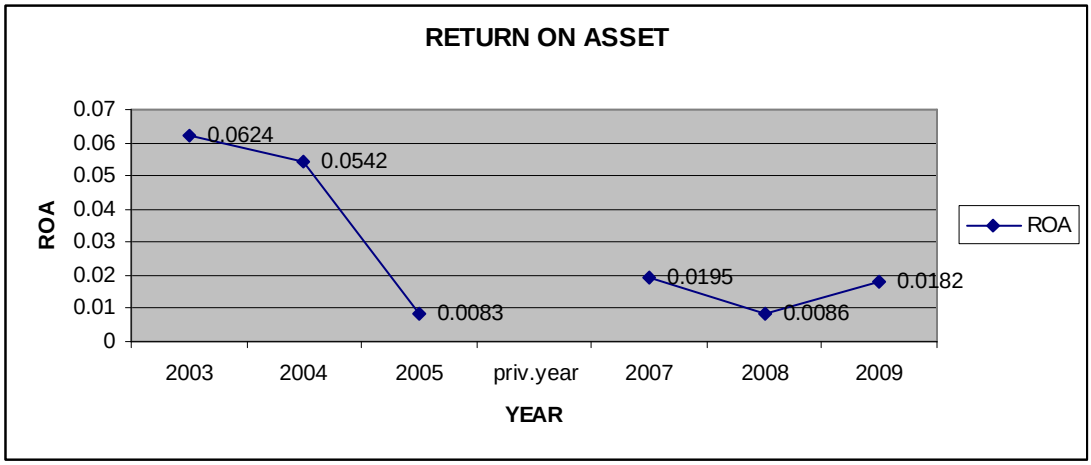
	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	significance	comment
Return on asset(ROA)	0.0154	0.0416	-0.02620	-1.448	0.285	*insignificant

Source: SPSS output.

***At 5 % significant level.**

Again, the above table reveals that mean value of ROA decline from 0.0416 before privatization to 0.0154 after privatization at 5% significant level even though it is statistically in significant. So this result indicates that the management of TASSCo was not efficient in using their asset to generate profit. The following line chart shows the trend of return on asset of the company over the year.

Fig 2, return on asset trend.



Source: financial statement of TASSCo

4.1.3 Return on equity (ROE)

one of the most important profitability metrics is return on equity (or ROE for short). Return on equity reveals how much profit a company earned in comparison to the total amount of shareholder equity found on the balance sheet.

A business that has a high return on equity is more likely to be one that is capable of generating cash internally. For the most part, the higher a company's return on equity compared to its industry, the better. But the reverse is true in case of Tikur Abay Shoe Share Company.
The following table shows the mean value of ROE before and after privatization, mean change, t-value and degree of significant level.

Table 4.3., Performance Indicator: ROE

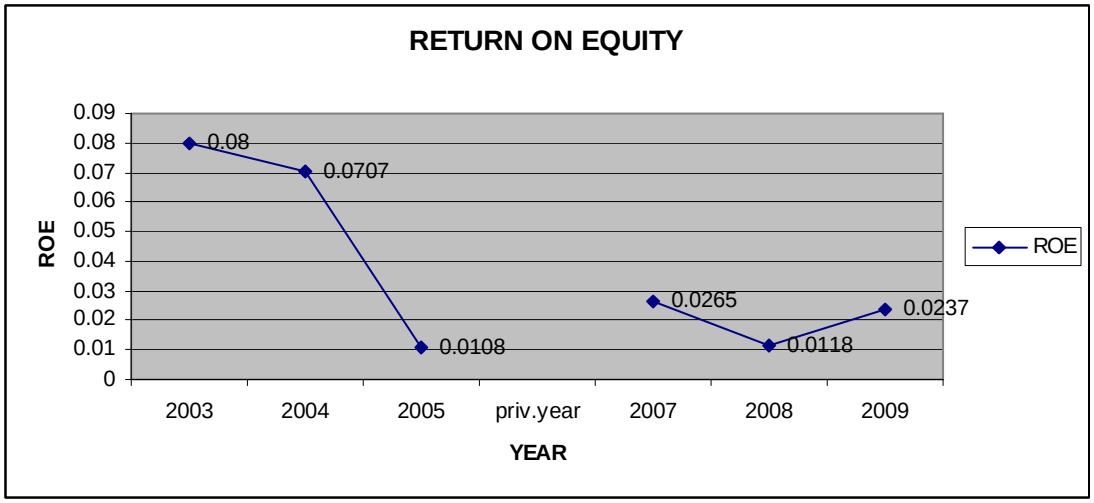
	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	Significance	comment
Return in equity(ROS)	0.0206	0.0538	-0.03328	1.373	0.303	*insignificant

Source: SPSS output.

*** At 5 % significant level.**

The last performance indicator of profitability is return on equity (ROE), this indicator also shows decline in the mean value from 0.0538 before privatization to 0.0206 following privatization. Similarly the declines hear is statistically insignificant. The following line chart shows ROE trend of the company.

Fig 3, return on equity trend.



Source: financial statement of TASSCo.

The researcher measures profitability by the return on sales, return on asset and return on equity ratios. Contrary to the privatization policy, the researcher result document deterioration following privatization. So that the researcher concludes that privatization doesn't bring any significant change on profitability of the company; which is totally against the one observed for developing countries by muggings et al. (1994).

The researcher investigates the following major problem that directly or indirectly affects the company's profitability following privatization.

The Company has marketing related problems that possibly affect the sales and profitability of a company. The main ones are:

- Poor product diversification

  Tikur Abay Shoe Share Company concentrates mainly on military bots even though it has potential to produce different models of civilian shoe. It is obvious in shoe industry that, within each broad category of footwear (children, ladies, gents' safety and military) there are different models, which offers better market than others. Working on product

diversification to achieve the highest market share is highly essential because the loss in one product line will be compensated by the gains on the other line, so that risk can be easily minimized.

- Weak product distribution system.

  According to the marketing department of TASSCo: The company have three shops in Addis Ababa, Mekelle and Hawassa one each and one product display in the Oromia Co-operatives, one in Merkeb Union in Amhara region to distribute their products to their final users. But the rest customers who are located in different part of Ethiopia do not have easy access to buy the offers of the company. So that, this can directly affects the company's sales volume and profitability.

- The company promotion system is very poor.

  As compared to other shoe companies Tikur Abay Shoe Share Company uses weak promotional tools; they use broachers and some times news papers to promote their products. According to the marketing department: till now the company didn't use broad cast media (TV, radio and website) this is because of the fact that the company do not allocate advertisement budget and they believe that the company have good image in the minds of customers.

- The company lacks experience and skill in designing competitive and fashionable products;

  The main reason for this is lack of modern and sophisticated machines so that TASSCo face difficulty to produce fashionable civilian shoes so as to satisfy the needs and wants of its customers. Since it is the era of globalization ; people's way of eating, drinking, dressing etc becoming similar .now a days many peoples were concerned about fashion especially in shoe, clothe and car .But the company fails to catch the hearts and minds of customers by producing fashionable and quality civilian shoes.

- The company lacks adequate skill and equipment to conduct quality control:

  This was a very big problem which is observed in the company; Quality is a built in characteristics of any production or service. Every work unit is responsible for producing or giving quality service as per the laid down quality standards and systems. Accordingly, the function of this work unit is to follow up and control whether the production process of the Share Company is run according to the set quality standards or not. Structurally, the service is supposed to have five job positions and twelve employees. The job positions are- Quality Control Service Head, Senior Quality Controller, Process Quality Controller, Laboratory technician, and Quality Control Clerk.

  However, at present, two of the above named job positions; the Quality Control Service Head and Laboratory Head job positions are not staffed. The total number of employees is also ten, including the senior quality controller who acts as the head of the service at present. The existence of a laboratory head per supposes the existence of an independent laboratory unit. However, the structure seems to have only a head with out laboratory equipments, Lab technician or other relevant job titles. There fore, the structure of this service needs to be analyzed as to its appropriateness and the existence of relevant job positions and man power strength.

4.2, Operating efficiency

Privatization is expected to result in increased efficiency in privatized enterprises as a result of new investment, new technology and improved corporate governance. The researcher computed two indicators of operating efficiency: sales efficiency (real sales/employees) and net income efficiency (net income/employees).

The following table will demonstrate the mean value of sales efficiency before and after privatization, mean change due to privatization, t- value and degree of significant level.

Table 4.4 Performance Indicator: Sales Efficiency

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	Significance	Comment
SALEFF	86396.52	63452.84	22943.68	1.373	0.303	*Insignificant

Source: SPSS output.

***At 5 % significant level**

Again the result here is also contrary to the prediction of the researcher; the mean value of SALEFF shows some sort of increment but still it is statistically insignificant at 5% significant level As per the result shown in the above table 4 the mean value of SALEFF (sales efficiency) of the company is birr 63453 before privatization and it increases to birr 86397 after privatization, the mean change is +22944 but the change is statistically insignificant.

The other indicator of operating efficiency is that of net income efficiency and it is calculated as net income/total employee.

The following table will demonstrate the mean value of net income efficiency before and after privatization, mean change due to privatization, t- value and degree of significant level.

Table 4.5, Performance Indicator: Net Income Efficiency

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	Significance	Comment
NIEFF	14227	30537	-16310	-1.210	0.350	*Insignificant

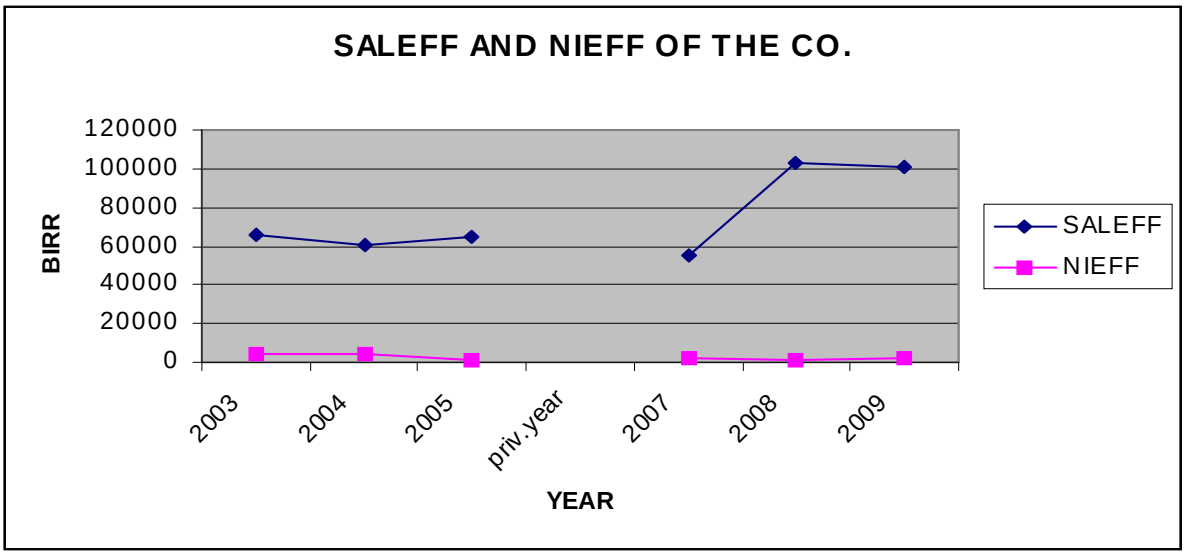
Source: SPSS output.

***At 5 % significant level**

According to the above table 4.5 net income efficiency ratio shows decline that is from birr 30537 before privatization to birr 14227 after privatization the mean change is birr -16310 but the change is again statistically insignificant.

The following line chart demonstrates the SALEFF AND NIEFF trend of TASSCo.

Fig 4, SALEFF AND NIEFF trend of the company



Source: financial statement of TASSCo.

Privatization is expected to result in increased efficiency in privatized enterprises as a result of new investment, new technology and improved corporate governance. But the reverse is true in case of TASSC0. So that the researcher concludes that privatization doesn't bring significant change in operating efficiency of Tikur Abay Shoe Share Company. The main cause for decline in net income efficiency is that company expense and cost of goods sold increases in relative to its sales following privatization. However the following problems were root causes that affect the overall operating efficiency of a company.

4.2.1, possible causes

As per finance department of Tikur Abay Shoe Share Company; the productivity in the company is not as such satisfactory after privatization. Based on this the researcher investigates the following possible causes that possibly affect the company's operating efficiency.

- **a.** The average age of employees is too high and high absenteeism
- **b.** Poor work handling techniques
- **c.** Poor supervision and
- **d.** Lack of modern technology and machines.

A, It is obvious that the best working years of a worker in an industry is between the ages of 18 - 40 years. But the case is different in Tikur Abay Shoe Company there are very small percentage of the total employees were between 18 - 38 years of age. There are however 84 employees over the age of 55 years these workers are not able to work as they were, this obviously has an impact on their ability to function efficiently and to their full potential as when they were young, and the absenteeism is mainly a result of being aged and it can possibly affect the operating efficiency of the company.

The following table shows employee profile by age category

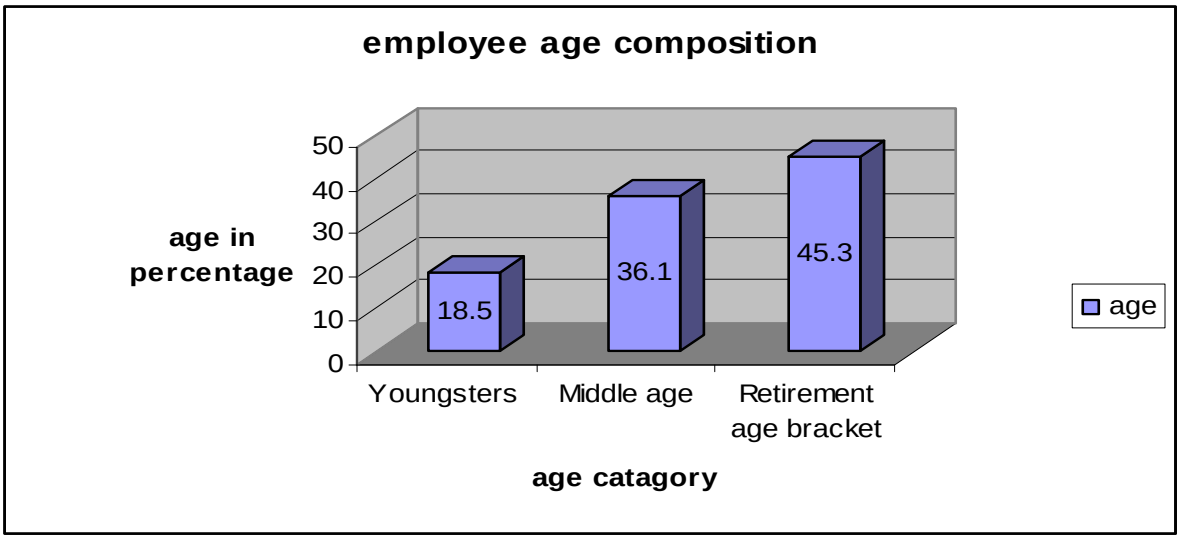
Table 4.6, Employee profile by age category

No	Age Group	Total	% From the Total
1	18-25	2	0.3
2	26-31	3	0.5
3	32-38	98	17.7
4	39-45	201	36.1
5	46-50	168	30.2
6	Above 50	84	15.1
TOTAL		**556**	**100**

Source: personnel department of the company.

Out of the total 556 employees only 103 employees were under active age group, 201 of 556 were in a middle age category and 252 employees out of 556 were under retirement age bracket. The following bar chart demonstrates the fact.

Fig 5, employee age compostion.



Source: personnel department of the company

The above bar chart shows the age composition of the employee of the company in the following proportion.

- Active age(18-38) =18.5%
- Middle age(39-45) =36.1%
- Retirement age bracket(> 45) =45.3%

It is highly known that workers in active age group are more productive than aged workers; but the above figure shows that 45.3 percent of the company's workers were under the retirement age bracket. So that this can highly affect the company's operating performance (productivity)

B, poor work handling is also another problem related with the poor supervision in most of the departments this poor work handling is related to the amount of time spent by both the supervisors and operators in the movement of work in all departments. There is too much time spent carrying work from one operator to another.

C, poor supervision is the other factor that affects the company's operating efficiency. As per personnel department head; some of the supervisors were not efficient in doing their day to day activities. So this can affect the quality of the work in each department.

D, Lack of modern technology and machines resulted poor productivity and limited scope for product diversification. The existing machineries of the company are too old as a result there is high spare part, repair and maintenance cost. In addition to this the existing machineries are not modern so that they are not suitable to produce modern civilian shoes. So this makes the company not to ensure better quality of the finished product, reduce production cost and became profitable.

4.3, capital investment

A capital investment is the acquisition of a fixed asset that is anticipated to have a long life of use before it has to be replaced or repaired.(http://www.investopidia.com). Two of the most easily recognizable examples of capital investments are land and buildings. However, a capital investment is made any time that a company purchases goods that will be benefit the operation of

the business, but will not be used to cover the operational costs of the business. Greater emphasis on efficiency is anticipated to lead newly privatized firms to increase their capital investment spending. Once privatized, firms should increase their capital expenditures since they have access to private debt and equity markets (Boubakri and Cosset, 1998).To assess the impact of privatization on capital formation, the researcher computes two indicators: capital expenditure to sales and capital expenditure to total assets. The following table will demonstrate the mean value of CAPEX/T.SALES before and after privatization, mean change due to privatization, t- value and degree of significant level.

Table 4.7, Performance Indicator: CAPEX/T.SALES

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	significance	Comment
Capital expenditure total sales	0.0972	0.0707	0.02643	0.885	0.469	*Insignificant

Source: SPSS output.

***At 5 % significant level**

The above table reviles that the mean value of capital expenditure to sales increases from0.0707 to 0.0972 however the increment is statistically insignificant at 5 percent significant level.

The following table will demonstrate the mean value of CAPEX/T.ASSET before and after privatization, mean change due to privatization, t- value and degree of significant level.

Table 4.8, Performance Indicator: CAPEX/T.ASSET.

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	significance	Comment
Capital expenditure to total asset	0.0633	0.0617	0.0016	0.045	0.969	*Insignificant

Source: SPSS output.

*** At 5 % significant level**

Capital expenditure to total asset ratio is also another ratio that helps to measure capital investment of the firm. According to the above table the mean value of the capital expenditure to total asset was increased from 0.0617(before privatization) to 0.0633(after privatization) however the increment is statistically insignificant at 5 percent level.

The result of the two ratios that are used to measure capital investment of the firm shows decline even though it is statically insignificant. The result observed in case of Tikur Abay Shoe Share Company is highly contrary to the expectation of the government and the hypothesis of the researcher because after privatization it is expected that privatized firm's improves their capital investment. The researcher tries to identify some of the major causes below.

- The company expansion and replacement programs (capital expenditure)

Capital expenditures (CAPEX or capex) are expenditures creating future benefits. A capital expenditure is incurred when a business spends money either to buy fixed assets or to add to the value of an existing fixed asset with a useful life that extends beyond the taxable year. Capex are used by a company to acquire or upgrade physical assets such as equipment, property,

or industrial buildings. Generally; capital expenditures are amounts spent on: Acquiring fixed assets fixing problems with an asset that existed prior to acquisition

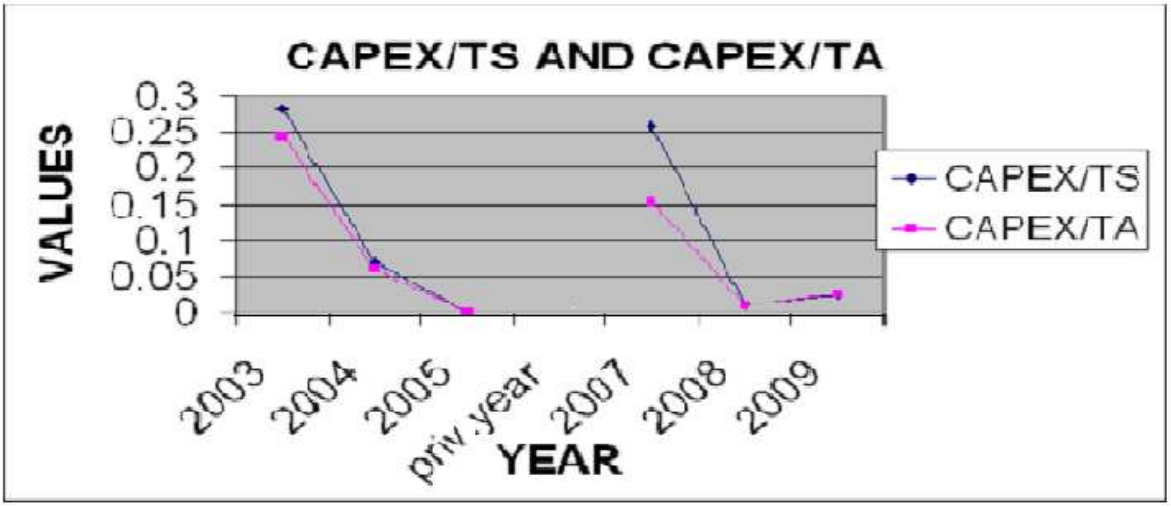
Preparing an asset to be used in business includes.

1. legal costs of establishing or maintaining one's right of ownership in a piece of property
2. restoring property or adapting it to a new or different use
3. starting a new business

Source :(http://en.wikipedia.org/wiki/)

But the capital expenditure used by the company to acquire or up grade physical assets like machineries, equipments, properties, land and others is not as such encouraging. That is why following privatization two of capital expenditure ratios shows decline. The following line chart demonstrates the capex/total sales and capex/total asset trend of TASSC0.

Fig 6, CAPEX/TS AND CAPEX/TA trend of the company.



Source: financial statement of the company

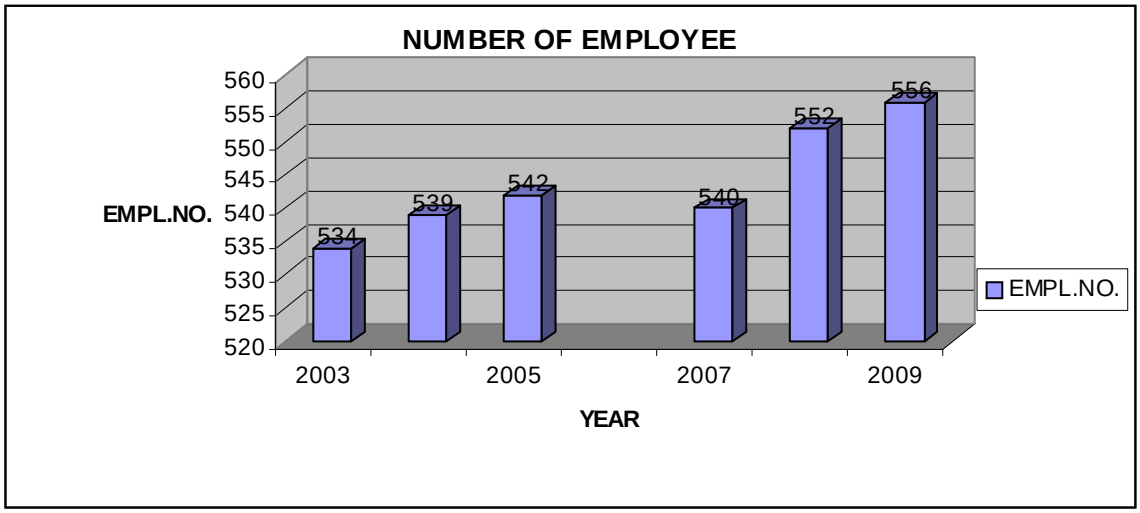
The above line chart shows that both the capital expenditure to total sales and capital expenditure to total asset of the company shows increment following privatization but it starts to decline in the year 2008 and 2009.So this is contrary to the hypothesis of the researcher and the expectation of the government (privatization objectives).

4.4, Employment change

One apprehension among government officials' regarding privatization is its potential negative impact on social stability should significant employment loss occur. Prior to privatization most state owned enterprises tend to be over staffed thus government expects large decline in employment levels following privatization .consequently, in order to increase efficiency layoffs would be expected. There for the research examine it by computing average employment levels for the three years periods i.e. 2003 to 2005(before privatization) and 2007 to 2009(after privatization) and testing whether employment falls after privatization.

The analysis shows an increase in employment of Tikur Abay Shoe Share Company that is from 542 before privatization to 556 following privatization. The mean before privatization is 539 then it increases to 550 after privatization, so that the mean change is about 11 and it is statistically insignificant at 5 % level. Again the result which is observed here is contrary to the prediction of the researcher and the expectation of the government because following privatization it is expected that privatized firms cut employment so as to be efficient. The following bar chart will show the trend of employment level of the company.

Fig 7, number of employees



Source: personnel department of the company

4.5, Change in leverage

Leverage means the amount of debt used to finance a firm's assets. A firm with significantly more debt than equity is considered to be highly leveraged. The researcher uses debt ratio to measure the firms leverage structure.

Debt ratio: A ratio that indicates what proportion of debt a company has relative to its assets. The measure gives an idea to the leverage of the company along with the potential risks the company faces in terms of its debt-load.

$$\text{Debt Ratio} = \frac{\text{Total Debt}}{\text{Total Assets}}$$

A debt ratio of greater than 1 indicates that a company has more debt than assets; meanwhile, a debt ratio of less than 1 indicates that a company has more assets than debt. Used in conjunction

with other measures of financial health, the debt ratio can help investors determine a company's level of risk. (http://www.investopedia.com)

The switch from public to private ownership should lead to a decrease in leverage because the governments removal of debt guarantee will increase the firms cost of borrowing and because the firm will have increase access to public equity market Megginson et al. (1994). Change in leverage is examined by observing change in total debt to total asset (TDTA). The following table will demonstrate the mean value of total debt/total asset before and after privatization, mean change due to privatization, t- value and degree of significant level

Table 4.9, Performance Indicator: Leverage

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t- value	significance	Comment
Total debt by total asset	0.2535	0.2271	0.02650	2.119	0.168	*Insignificant

Source: SPSS output.

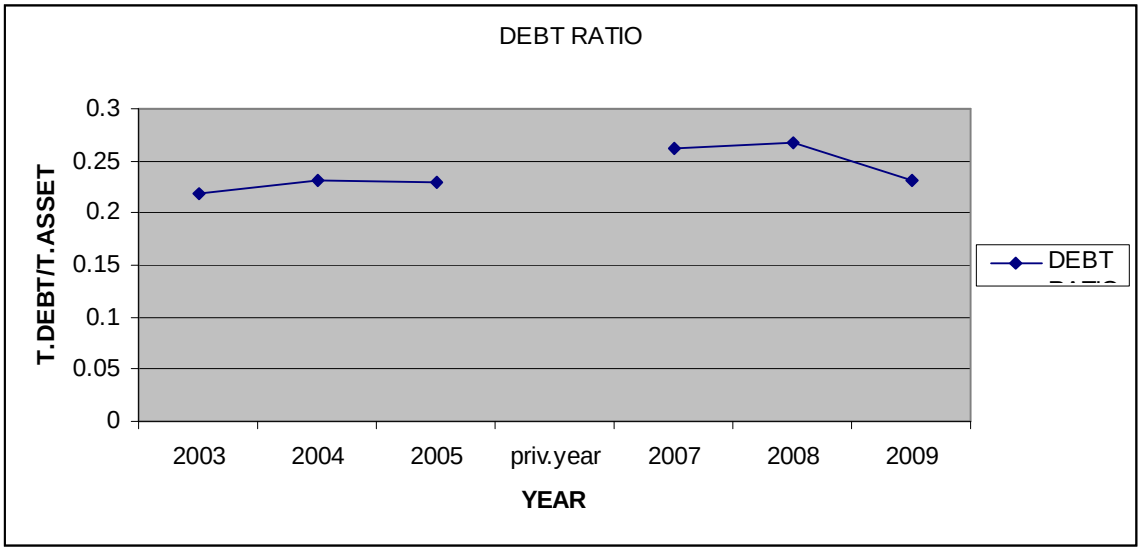
*** At 5 % significant level**

Again the result is contrary to the prediction of the researcher and privatization policy; leverage increases following privatization in TASSCo. The mean increases from 0.2271 to 0.2535 following privatization. But the change is statistically insignificant at 5 percent level. SOEs, particularly in developing countries, are typically encumbered by large debts, causing many to have negative net worth. Private buyers often make it clear that they do not want to take on these debts, even when the sale price is discounted by the amount of the debt. They seek an immediate positive cash flow to reduce their risk and help finance new investment. Debt write-downs are thus not uncommon practices for divesting governments the world over. MNR (1994) and

Boubakri and Cosset (1998) show that leverage decreases Significantly after privatization, a result that is partly due to debt write-downs and partly to infusions of equity capital into those firms executing primary offerings, but mostly a result of higher (retained) profitability. A priori, the shift from public to private ownership should lead to a decrease in leverage because the government's removal of debt guarantee will increase the cost of borrowing.

The following line chart displays the trend of total debt to total asset of TASSCo.

Fig 8, debt ratio trend



Source: financial statement.

As per the above line chart; the debt ratio of the company after privatization shows some increment in the year 2007 and 2008 but it is statistically insignificant and it starts to decline in the year 2009. So this indicates that a company debt has increases with respect to its assets this is due to the fact that the company was highly depending on debt finance to run its business. Again TASSCo's share holders want to use the existing fixed asset of a company rather than investing money in new one. The reason as per finance department head is that almost all machines that are used in shoe industry were too costly and again the company have high depreciation cost.

So that this two basic reasons makes the company total debt in relation to its total asset to increase even following privatization.

4.6, liquidity

Liquidity Ratios:

The liquidity of a firm is measured by its ability to satisfy its short-term obligations as they come due (Gitman, 2004). Liquidity also stands for ability of a company to convert its assets into cash quickly and with lower costs as possible. Such liquid assets are necessary to cover any "financial emergencies" and play as a buffer in company's operations. Liquidity ratios reflect the short-term financial strength/solvency of a company.

The liquidity of a business firm is usually of particular interest to its short-term creditors since the liquidity of the firm measures its ability to pay those creditors.

Several financial ratios measure the liquidity of the firm. But the researcher considered only current ratio to measure the liquidity position of the company.

Current Ratio: The current ratio, one of the most commonly cited financial ratios, measures the company's ability to meet its short-term obligations by using only current assets. The current assets consist of cash and assets that can easily be turned into cash and the current liabilities consist of payments that a company expects to make in the near future. Thus, the ratio of the current assets to the current liabilities measures the margin of liquidity. It is known as the current ratio. The current ratio is probably the best known and most often used of the liquidity ratios.

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

The following table shows the mean value, mean change due to privatization, t-value and degree of significance of Current ratio.

Table 4.10, Performance Indicator: Current Ratio

	Mean value after privatization	Mean value before privatization	Mean change due to privatization	t-value	Significance	Comment
C.asset/C.libility	1.9425	3.0351	1.0926	1.430	0.289	*Insignificant

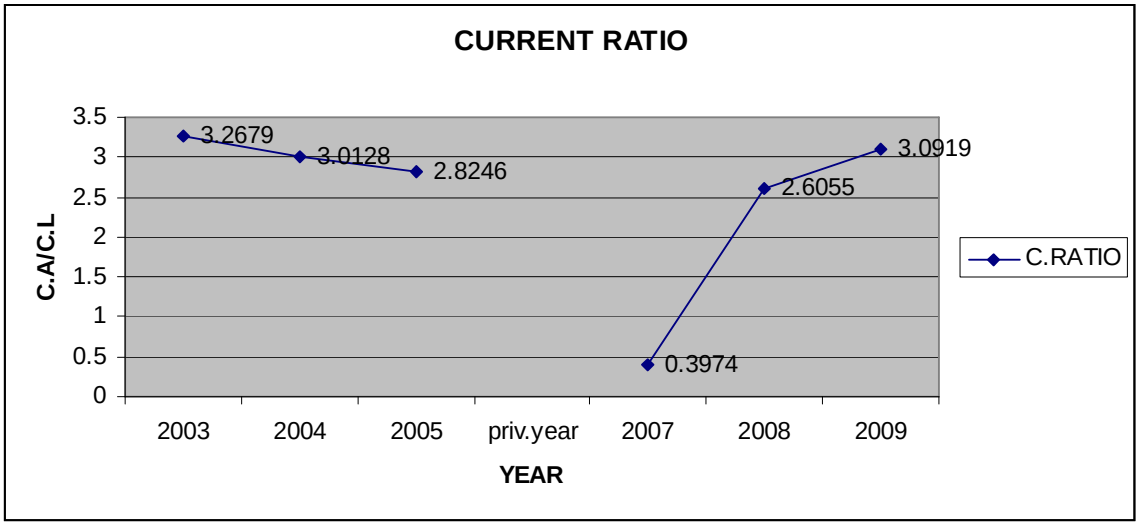
Source: SPSS output.

***At 5 % significant level**

According to the above table the mean value of current asset of the company before privatization is 3.0351 then it declines to 1.9425 after privatization. But the decline is statistically insignificant at 5 percent significant level.

The following line chart will show the trend of the current ratio of the company before and after privatization.

Fig 9, current ratio trend



Source: financial statement of TASSCo.

As per the above line chart the financial ratio in the year 2007(after privatization) is 0.3974 which is the highest decline in the history of the company. The mean decline following privatization is 1.0926; this decline is because of the fact that current asset of the company declines in relation to current liability of the company and vice-versa.

Chapter v: Conclusion and Recommendations

Conclusions

Although privatization has turned in to world phenomena, it is only recently that Ethiopia has launched privatization programs. This paper compares the pre and post financial and operating performance of Tikur Abay Shoe Share Company. Financial ratios were calculated as average of three years before and after privatization. this are profitability(return on sales ,return on asset and return on equity),operating efficiency(sales efficiency and net income efficiency),capital investment(capital expenditure to sales and capital expenditure to total asset),leverage(total debt to total asset), employment(total number of employee),liquidity(current asset to current liability). Furthermore t-test statistics is used to identify mean values, mean change, t-value and degree of significant.

I, Changes in Profitability

Profitability is the most important indicator to measure the performance of firms. So as to measure profitability; return on sales, return on asset and return on equity are employed and the result is decline in mean value of the three indicators following privatization but the decline is statistically insignificant. The result is contrary to the expectation of the government and the prediction of the researcher. This is due to many reasons, the main once are; The average age of employees is too high and there is high absenteeism, Poor work handling techniques and lack of skill, Poor supervision and Lack of modern technology and machines resulted poor productivity, limited scope for product diversification and The company lacks adequate skill and equipment to conduct quality control. So this and other related problems affect the company operating efficiency.

II, Changes in operating efficiency

Privatization is expected to result in increased efficiency in privatized enterprises as a result of new investment, new technology and improved corporate governance. The researcher computed two indicators of operating efficiency: sales efficiency (real sales/employees) and net income efficiency (net income/employees). Again the result is contrary to the prediction; the mean value of SALEFF shows some sort of increment from birr 63453 before privatization to birr 86397 after privatization, but the increment is statistically insignificant at 5 percent level.

Net income efficiency ratio (NIEFF) is another measure of operating efficiency ratio and it shows decline following privatization; the mean value of NIEFF decreases from birr 30537 before privatization to birr 14227 after privatization but again the change is statistically insignificant. The government expects operating efficiency will significantly increases after privatization. But the result is contrary to the expectation of the government and the prediction of the researcher. This is due to many reasons, the main once are the following;

The average age of employees are too high and there is high absenteeism, Poor work handling techniques and lack of skill, Poor supervision and Lack of modern technology and machines resulted poor productivity, limited scope for product diversification, The company lacks adequate skill and equipment to conduct quality control and lack of experience and skill in designing competitive and fashionable products because of lack of modern technology; So this and other related problems affect the company operating efficiency.

III, Changes in Capital investment

A capital investment is the acquisition of a fixed asset that is anticipated to have a long life of use before it has to be replaced or repaired. To assess the impact of privatization on capital formation, the researcher computes two indicators: capital expenditure to sales and capital expenditure to total assets.

The result of both capex/total sales and capex/total asset after privatization shows some increment. That is the mean value of capital expenditure to sales increases from0.07072 to 0.0972 however the increment is statistically insignificant at 5 percent significant level. Again the mean value of the capital expenditure to total asset shows increment i.e. from 0.0617 to 0.633 but the increment is statistically insignificant at 5 percent level.

IV, Employment change

One apprehension among government officials' regarding privatization is its potential negative impact on social stability should significant employment loss occur**.** Prior to privatization most state owned enterprises tend to be over staffed .thus government expects large decline in employment levels following privatization. TASSCo has 542 employees and it grows to 556 following privatization. And according to t-statistics the mean value before privatization is 539 then it increases to 550, so that the mean change is about 11 and it is statistically significant at 5 % significant level. Again the result which is observed here is contrary to the expectation of the government. The number of employee in the company significantly increases following privatization.

V, Change in leverage

Leverage means the amount of debt used to finance a firm's assets. A firm with significantly more debt than equity is considered to be highly leveraged. The researcher uses debt ratio to measure the firms leverage structure. Researchers like:

MNR (1994) and Boubakri and Cosset (1998) show that leverage decreases significantly after privatization, a result that is partly due to debt write-downs and partly to infusions of equity capital into those firms executing primary offerings, but mostly a result of higher (retained) profitability. A priori, the shift from public to private ownership should lead to a decrease in leverage because the government's removal of debt guarantee will increase the cost of borrowing.

But Contrary to the researcher's prediction the leverage of Tikur Abay Shoe Share Company found to be increase following privatization. The mean value increases from 0.2271 to 0.2535 but the increment is still statistically insignificant at 5 percent significant level. This is due to the decrease of the company (retained earnings) profitability.

VI, Changes in Liquidity

Several financial ratios measure the liquidity of the firm. Those ratios are the current ratio, the quick ratio or acid test, cash ratio and net working capital. But the researcher considered only current ratio to measure the liquidity position of the company. As a result:

The mean value of current ratio of the company before privatization is 3.0351 then it declines to 1.9425 after privatization. But the decline is statistically insignificant at 5 percent significant level. Again this is also contrary to the expectation of the government. Since it is expected that privatization increases the liquidity position of a company. Generally the researcher concluded that privatization didn't bring any improvement in financial and operating performance of Tikur Abay Shoe Share Company (TASSC0.).

Recommendations

In line with the analysis and findings presented in chapter four, the following recommendations are made.

- Tikur Abay Shoe Share Company concentrates mainly on military bots even though it has potential to produce different models of civilian shoe. therefore in order to maximize profitability and satisfy customers needs TASSCO should also give attention to all categories of footwear like children, ladies, gents' safety and military so that the risk can be easily minimized because the lose in one category can be compensated with the gains in other one.

- In order to serve all customers who are located in different part of Ethiopia TASSCO should maximize the number of outlets in all locations. So that each and every customers can easily access the offers of the company. So that the company will have large market share than similar footwear companies in the country.

- The management of TASSCO should allocate advertisement budget so as to advertise its offers through TV, RADIO, and other print Medias (magazines, newspapers and broachers). In addition to this the company should develop its own website so that it can easily promote its products to allover the world thereby attain international competitiveness.

- The company should purchase modern and sophisticated machines that are suitable to produce different designs of fashionable and quality civilian shoes. In that way the company can satisfy the needs and wants of its customers. In addition to this the company can also minimize spare part, repair and maintenance costs for old machiens.

- The management of TASSCO should staff two job positions (the Quality Control Service Head and Laboratory Head together with lab technician and different lab equipments. So that the company can assure quality control.

- In order to improve the operating efficiency of the company the management of TASSCO Should train and employ new young workforce for each employee under retirement age bracket.

- In order to minimize time spent in carrying out work from one operator to another, the company should assign appropriate supervisors and fulfill necessary equipments that can facilitate the smooth workflow.

- Both capital expenditure ratios (capex/sales and capex/asset) of a company became below zero following privatization, so this indicates that the company doesn't invest on fixed

assets after privatization. It is highly recommended that the company management should invest on fixed asserts like machineries, building and different equipments that are anticipated to have a long life of use.

- TASSCO doesn't cut employment as expected following privatization rather it increases from 542(before privatization) to 556 (after privatization). But surprisingly; above 45 percent of employees were under retirement age bracket. There fore in order to be efficient and cost effective; the company should cut those employees with in retirement age and repels them with skillful and energetic workforce.

- Contrary to the expectation of the government; the study shows increment in leverage even though it is statically insignificant. The mean increased from 0.2271 to 0.2535 following privatization. Therefore TASSCO shouldn't highly depend on debt finance to run its business because large debts can cause the company to have negative net worth.

- The researcher considered current ratio to measure the liquidity position of the company as a result the mean value decreases from 3.0351 to 1.9425 following privatization even though the decline is statically insignificant at 5 percent level. So that it is highly recommended that TASSCO should have higher liquidity position (should have asset that can be easily convertible in to cash) so that they can easily cover any financial emergencies at any time.

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Proclamation No.146/1998 about policy making and monitoring function, to enhance managerial efficiency, cost effectiveness and innovation in business activity

Proclamation No 87/1994 about the establishment of Ethiopian privatization agency.

Proclamation No 193/2000 about the power of Ethiopian privatization agency.

Annex I: Balance Sheet of TASSCo

TIKUR ABAY SHOE SHARE COMPANY
BALANCE SHEET
AT 30 JUNE 2004

	Notes	Birr	Birr	2003 Birr
ASSETS EMPLOYED				
PROPERTY, PLANT AND EQUIPMENT	1 b), 2		11,474,387	11,551,868
CURRENT ASSETS				
Stock	1 b), 3	20,262,003		14,343,894
Income tax recoverable	4	505,481		139,308
Debtors	5	5,146,920		14,301,184
Cash and bank balances		815,826		135,257
		26,730,230		28,919,643
CURRENT LIABILITIES				
Creditors	6	3,365,856		6,013,173
Bank overdraft	7	2,729,657		2,836,318
Dividend payable	8	2,776,579		-
		8,872,092		8,849,491
NET CURRENT ASSETS			17,858,138	20,070,152
			29,332,525	31,622,020
FINANCED BY				
SHARE CAPITAL	9			
Authorized and paid: 22,053 shares at Br 1,000 each			22,053,000	22,053,000
CAPITAL RESERVE	10		2,547,886	2,547,886
LEGAL RESERVE	11		854,943	751,337
ACCUMULATED PROFIT			1,866,887	3,223,483
			27,322,716	28,575,706
PROPOSED DIVIDENDS	12		1,968,519	2,999,138
TOTAL EQUITY			29,291,235	31,574,844
DEFERRED TAX LIABILITY	13		41,290	47,176
			29,332,525	31,622,020

The notes on pages 6 to 15 form an integral part of these financial statements.

2

TIKUR ABBAY SHOE SHARE COMPANY
BALANCE SHEET
AT 30 JUNE 2005

	Notes	Birr	Birr	2004 Birr
ASSETS EMPLOYED				
PROPERTY, PLANT AND EQUIPMENT	1 b), 2		13,356,458	11,474,387
CURRENT ASSETS				
Stock	1 b), 3	21,660,424		20,262,003
Income tax recoverable	4	1,006,598		505,481
Debtors	1b), 5	1,797,246		5,146,920
Cash and bank balances		248,694		815,826
		24,712,962		26,730,230
CURRENT LIABILITIES				
Creditors	6	3,288,434		3,365,856
Bank overdraft	7	3,382,254		2,729,657
Dividend payable	8	1,776,579		2,776,579
State dividend	1b)	181,023		—
Industrial development fund	1b)	120,681		—
		8,748,971		8,872,092
NET CURRENT ASSETS			15,963,991	17,858,138
			29,320,449	29,332,525
FINANCED BY				
SHARE CAPITAL	9			
Authorized and paid: 22,053 shares at Br 1,000 each			22,053,000	22,053,000
CAPITAL RESERVE	10		2,547,886	2,547,886
LEGAL RESERVE	11		870,822	854,943
ACCUMULATED PROFIT			1,866,887	1,866,887
			27,338,595	27,322,716
PROPOSED DIVIDENDS	12		1,968,519	1,968,519
TOTAL EQUITY			29,307,114	29,291,235
DEFERRED TAX LIABILITY	1b), 13		13,335	41,290
			29,320,449	29,332,525

The notes on pages 6 to 16 from an integral part of these financial statements.

2

TIKUR ABBAY SHOE SHARE COMPANY
BALANCE SHEET
AS AT 30 JUNE 2007

CURRENCY: BIRR

ASSETS EMPLOYED	**Notes**			**2006**
Property, plant & equipment	2b,i , 3		8,711,129	11,557,890
Deferred tax asset			120,428	120,428
Good will	4, 2b		8,229,885	
CURRENT ASSETS				
Inventory	5	24,453,610		20,972,917
Income tax recoverable	6	620,564		1,189,138
Trade & other receivables	7	7,700,438		8,628,621
Cash and bank balances	8	346,201		459,526
			33,120,813	31,250,202
Total assets			**50,182,255**	**42,928,520**
EQUITY AND LIABILITIES				
Capital and reserve				
Capital				
Authorized and paid				
3,500 shares of 8,776 each	9	30,716,000		22,053,000
Capital reserve	10	2,547,886		2,547,886
Legal reserve	11	900,059		900,059
Accumulated profit		886,161		1,866,887
Proposed dividends	12	1,968,519		1,968,519
			37,018,625	29,336,351
CURRENT LIABILITIES				
Trade and other payable	13	3,832,473		4,225,992
Bank overdraft	14	6,697,363		6,732,383
Dividend payable		2,109,886		2,109,886
Industrial development fund		342,885		342,885
State dividend		181,023		181,023
			13,163,630	13,592,169
Total equity & liabilities			**50,182,255**	**42,928,520**

2

TIKUR ABBAY SHOE SHARE COMPANY
BALANCE SHEET
AS AT 30 JUNE 2008

CURRENCY: BIRR

ASSETS EMPLOYED	Notes			2007
Property, plant & equipment	2b,i , 3		8,121,505	8,711,129
Deferred tax asset			143,901	120,428
Good will	4, 2c		7,363,585	8,229,885
CURRENT ASSETS				
Inventory	5	30,083,505		24,453,610
Income tax recoverable	6	1,234,310		620,564
Trade & other receivables	7	4,196,701		7,700,438
Cash and bank balances	8	47,545		346,201
			35,562,061	33,120,813
Total assets			**51,191,052**	**50,182,255**
EQUITY AND LIABILITIES				
Capital and reserve				
Capital				
Authorized and paid				
3,500 shares of 8,776 each	9	30,716,000		30,716,000
Capital reserve	10	2,547,885		2,547,886
Legal reserve	11	900,059		900,059
Accumulated profit	12	1,409,666		886,161
Proposed dividends	13	1,968,519		1,968,519
			37,542,129	37,018,625
CURRENT LIABILITIES				
Trade and other payable	14	5,463,386		3,832,473
Bank overdraft	15	5,551,744		6,697,363
Dividend payable		2,109,886		2,109,886
Industrial development fund		342,885		342,885
State dividend		181,022		181,023
			13,648,923	13,163,630
Total equity & liabilities			**51,191,052**	**50,182,255**

2

TIKUR ABBAY SHOPE SHARE CO

BALANCE SHEET

AS AT 30TH JUNE 2009

	Notes	Amount Birr	Amount Birr
FIXED ASSET			
Historical Cost	2	28,708,175.80	
Accum. Depreciation	2,1A	(20,922,126.40)	
Net Fixed Asset			**7,786,049.40**
Deferred tax asset			
Good Will	2	8,663,000.00	
Accum. Amoritzation	3,1B	(2,165,715.00)	
Net Good Will			**6,497,285.00**
			14,283,334.40
CURRENT ASSETS			
Stock	4	24,605,761.26	
Income tax recoverable	5	2,503,530.55	
Trade & other debtors	6	8,816,391.90	
Cash & bank balances	20	424,162.22	
			36,349,845.93
TOTAL ASSETS			**50,633,180.33**
EQUITY AND LIABILITIES			
Capital	10	30,716,000.00	
Capital Reserve	11	2,547,885.69	
Legal Reserve	12	946,070.95	
Accumulated Profit	16	2,698,598.77	
Proposed Dividend	17	1,968,519.00	
			38,877,074.41
CURRENT LIABILITIES			
Trade & Other payable	7	5,043,159.88	
Bank Overdraft	8,20	2,587,158.18	
Dividend Payable	13	2,141,543.08	
Industrial Development Fund	14	342,885.00	
State Dividend	15	181,022.20	
Tax payables		1,460,337.58	
			11,756,105.92
TOTAL EQUITY AND LIABILITIES			50,633,180.33

TASSC

Annex II: profit and loss account of TASSCo.

TIKUR ABAY SHOE SHARE COMPANY
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2004

	Notes	Birr	Birr	2003 Birr
SALES	1 d)		32,560,715	34,925,765
COST OF PRODUCTS SOLD	14		27,692,055	28,309,718
GROSS OPERATING PROFIT			4,868,660	6,616,047
OTHER INCOME	15		1,449,938	93,649
			6,318,598	6,709,696
EXPENSES				
Administration	16	2,101,890		1,773,895
Selling and distribution	17	1,149,400		991,563
Land and building taxes: 1975 - 2003		475,594		-
Financial charges		113,136		53,013
Directors' fees		27,800		8,045
Audit fee		20,000		18,000
Contribution to drought relief		13,770		250,000
Provision for stock obsolescence		-		363
Provision for doubtful debts		-		3,992
			3,901,590	3,098,871
NET PROFIT BEFORE TAXATION			2,417,008	3,610,825
TAX EXPENSE	21		344,883	1,084,554
NET PROFIT AFTER TAXATION			2,072,125	2,526,271

The notes on pages 6 to 15 form an integral part of these financial statements.

3

TIKUR ABBAY SHOE SHARE COMPANY
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2005

	Notes	Birr	Birr	2004 Birr
SALES	1 d)		34,983,376	32,560,715
COST OF PRODUCTS SOLD	14		31,413,159	27,692,055
GROSS OPERATING PROFIT			3,570,217	4,868,660
OTHER INCOME	15		330,345	1,449,938
			3,900,562	6,318,598
EXPENSES				
Administration	16	2,148,898		2,101,890
Selling and distribution	17	1,043,404		1,149,400
Land and building taxes: 1975 - 2003		-		475,594
Financial charges		279,651		113,136
Directors' fees		25,225		27,800
Audit fee		20,000		20,000
Contribution to drought relief		-		13,770
			3,517,178	3,901,590
NET PROFIT BEFORE TAXATION			383,384	2,417,008
TAX EXPENSE	21		65,801	344,883
NET PROFIT AFTER TAXATION			317,583	2,072,125

The notes on pages 6 to 16 form an integral part of these financial statements.

TIKUR ABBAY SHOE SHARE COMPANY
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2007

CURRENCY: BIRR

	Notes			2006
SALES			29,753,820	30,749,816
LESS: COST OF GOODS SOLD	15		(28,254,025)	(30,712,493)
GROSS OPERATING PROFIT			1,499,795	37,323
OTHER INCOME	16		1,324,189	4,296,185
			2,823,984	4,333,508
EXPENSES				
Administration	17	2,111,985		2,061,457
Selling & distribution	18	903,013		1,051,701
Financial charges	19	310,938		342,445
Directors fees		22,175		28,200
Provision for doubtful debts		3,484		6,674
Audit fee		20,000		20,000
Amortization		433,115		
			(3,804,710)	(3,510,477)
NET PROFIT BEFORE TAXATION			(980,726)	823,031
TAX EXPENSE			-	(238,283)
NET (LOSS)/PROFIT AFTER TAXATION			**(980,726)**	**584,748**

TIKUR ABBAY SHOE SHARE COMPANY
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2008

CURRENCY: BIRR

	Notes			2007
SALES			56,807,274	29,753,820
LESS: COST OF GOODS SOLD	16		(50,388,959)	(28,254,025)
GROSS OPERATING PROFIT			6,418,315	1,499,795
OTHER INCOME	17		93,202	1,324,189
			6,511,517	2,823,984
EXPENSES				
Administration	18	2,601,634		2,111,985
Selling & distribution	19	1,219,104		903,013
Financial charges	20	404,579		310,938
Directors fees		-		22,175
Provision for stock obsolescence		526,236		3,484
Audit fee		35,000		20,000
Amortization		866,300		433,115
			(5,652,853)	(3,804,710)
NET PROFIT BEFORE TAXATION			858,664	(980,726)
PROVISION FOR PROFIT TAX			(415,470)	-
NET PROFIT AFTER TAXATION			**443,194**	**(980,726)**

3

Tikur Abbay Shoe share co.

Profit & Loss Statement

For the period ended 30th June 2009

	Notes	Amount	Amount
Net Sales	9		56,457,441.00
Cost of Products Sold	24		50,566,312.87
Gross Operating Income			**5,891,128.13**
Other Income	21		267,318.27
			6,158,446.40
Operating Expenses:			56,724,759.27
Administrative		3,470,835.08	56,724,759.06
Selling & Distribution		1,052,248.22	
Interest	22	220,612.08	
Directors' Fee			
Audit Fee		8,275.00	
Provision for Stock Obsolescence			
Provision for bad Debts			4,751,970.38
Net Profit before taxation			**1,406,476.02**
Provision for taxation			486,236.79
Net profit(Loss) after taxation			**920,239.23**
Legal Reserve			46,011.96
Unapportioned Profit			874,227.27

TASSC