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Impact of Privatization on Firm's Performance: A Case of banking Sector of Pakistan

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Abstract

A mode of modifying assets and processes to the private sector from the public sector is identified as Privatization. Privatization is a valuable process to enhance the performance of firms. Many researchers have conducted the study to evaluate the impact of privatization on firm's performance by using different techniques. Prior researches show positive and negative impacts of privatization on firm's performance. This research has been conducted in order to find the influence of privatization on bank's performance in Pakistan. The research shows that privatization has constructive impacts on the performance of banks in Pakistan. A relative study was conducted in order to find the profitability, leverage and earnings per share, of privatized banks (MCB and ALB) and public sector banks (NBP and FWB) to evaluate the difference in performance of both. The data has been collected during the period of 2009-2014. Financial ratios has been calculated to evaluate the performance and represented by graph. Software SPSS (statistical package for social science) is being used for finding descriptive statistics and graphical analysis. The result shows that Privatized banks are more profitable than public sector banks over the span of six years. Research also reveals that privatized banks has upright outlook for future than public sector banks.

Keywords: *Privatization, bank's performance, profitability, leverage, earnings per share, Muslim Commercial bank (MCB), Allied bank (ALB), National bank of Pakistan (NBP), First Women bank (FWB), Pakistan.*

1. Introduction

As privatization can be termed as universal phenomenon, many markets in early 1990's which includes Eastern Europe and Russia have turned their economies from public proprietorship to market centered system. As the corporate world is becoming active gradually, a need has been recognize for the significance of the privatization and the effect of liberalization on the business sphere. A method of altering assets and processes to the private sector from the public sector is identified as Privatization. It is also a significant element that enables markets to operate appropriately. This forceful atmosphere in the business division has given rise to the rivalry and proficiency between the organizations. The higher the measure of completion between the businesses, the more the organizations tend to be competent. Privatization advances to economic development, growth in output, efficiency in exploitation of resources and increase in production and employment. In Pakistan, during the rule period of Prime Minister Nawaz Sharif in 1990's, developments were made to transfer the ownership of nationalized businesses to private sectors. In order to reduce managerial expenditure of the government privatization of firms were prepared.

This study is conducted to critically analyze the positive and negative impacts of privatization on firm's performance running in Pakistan. The performance of the firm will be measured through its profitability, level of leverage and earnings per share. As transfer of public businesses to private ownership is one of a study that extents curiosity for researchers, stakeholders and government. Numeral studies have been completed on this topic. But this study has its own significance because it covers competition in terms of profitability, leverage and earnings per share of firm.

1.1 Problem Statement

The primary objective of the study is to determine the incentives achieve by firm after privatization in terms of profitability, leverage and earnings per share.

1.2 Significance of the Study

Privatization helps economies and businesses to prosper and become efficient up to some extent. In recent years it has been an area of interest of many researches. Different variables have different effects on privatization of firm. This research will help in finding the impacts of privatization on profitability, leverage and earnings per share of the firm.

1.3 Objectives of the Study

In Pakistan the privatization is prepared to acquire better financial position and productivity. The main objectives of this study to inspect the impact of firm's privatization on its performance

Following are the objectives of the study;

- To assess the effect of privatization on the profitability of firm.
- To assess the effect of privatization on the level of leverage of the firm.
- To assess the effect of privatization on the earnings per share of the firm.

1.4 Limitation of the Study

Privatization is a significant process adopted by government in situation. The limitation of the study was that the access to data was restricted to some extent. There are numerous other variables that can be taken for study which are changes in wage structure, employee happiness and customer satisfaction. Privatization is a vast topic and to cover its potential variables the time of the study was short in order to have more optimal results.

1.5 Scope of the Study

The extensive significance of privatization processes cannot be neglected as it brings efficiency and productivity to firm's performance and enhance economic boost. It helps reduce government expenditure. This paper will helps in future to have deep insight about privatization.

2. Literature Review

(J. David Brown, 2006) Has estimate the effect of privatization on nationalized manufacturing firms in four economies (Hungary, Romania, Russia, and Ukraine) in this paper. Substantial number of firms is observed before and after privatization in this research. The study revolves around the estimation of long-run impacts of privatization and pre privatization selection bias. The findings strongly support the view that privatization matters, and they provide some evidence that the method of privatization matters as well.

A study by (Khalid, 2006) was an effort to inspect the outcomes of privatization and liberalization on the performance of the banking sector in Pakistan, using the CAMELS framework of financial indicators between the periods 1990-2002. Public sector banks, privatized banks, domestic private bank and foreign banks are observed in this study. The results obtained show little evidence of improvement in most of the indicators of financial health as a result of the privatization and liberalization policies pursued so far in the banking sector of the country.

The possession structure (Private or Public) has powerful impact on firm's financial performance. (Muhammad Fahad Siddiqi, 2012) investigate the impact of privatization on the company's financial performance and the performance of its stock. The study observes the performance of Pakistan telecommunication limited (PTCL) particularly. Results imply that there is a significant outcome of privatization on the average share prices, volume and number of trades, by showing positive impact. But the stock returns are not considerably influenced from the privatization. Investigation of the financial statistics proves deterioration in the monetary performance of the company after privatization dignified by operating profit margin, net profit margin, return on equity and earnings per share ratio.

In the paper (Filipovic, 2005) has analyzed the outcomes and the influence of privatization on the pace of economic growth, encouraged by the idea of people responding to benefits. A sample of 90 developing countries is used for this study. Analysis of privatization suggests that incentives allow a major role in the potential accomplishment of privatization as a feature of economic growth. In fact, privatization, accompanied by suitable structural reforms, creates benefits to progress economic efficiency, boost investment, and adopt latest technologies.

(Ahmed, 2014) set a study to found the result of privatization on the financial performance of the Kenyan aviation industry, particularly to the Kenya Airways Limited. The financial performance of Kenya Airways before and after its privatization was analyzed by financial statements throughout this phase. The sample of 37 staff was used in the study. The result of the study proved that there were positive developments in the performance of Kenya Airways afterward denationalization in terms of liquidity and liability ratios compared to its performance earlier privatization. This performance indicator showed also a boost in financial efficiency. It was found that profitability and financial efficiency increase after privatization.

(Javad Shahraki, 2011)Conduct a study to find the relationship among privatization and economic growth in Iran. For the research they use quarterly statistics of Iranian central bank for the period of 1989q1-2007q4.Competitiveness and the oil revenues importation is used as valuable dependent variables on the Iranian economic growth. The result of the study implies that privatization practice in Iran in short run is considerable. The main spot of the study is that revenues generated through oil in both short span and long span is major, which shows that privatization process doesn't facilitate to Iranian economic growth.

The study by (Muhammad Rizwan, 2015) critically compares the impact of privatization on Muslim Commercial Bank and Allied Bank of Pakistan. For this purpose the data has been collected from the Post Privatization Era (2008-2012) and compared with the Pre Privatization Era (1987-1991). The two major variables of the study were efficiency and financial Growth of the banks. The performance of two banks MCB and ABL were compared and evaluated. It is appreciably marked from the observed figures that privatization is a helpful in the prosperity of banks and ultimately for the nation.

Privatization is exercised by the governments to support the financial health and profitability of the firms. Many researchers believe that privatization of banks helps to advance financial position. In the paper (Alam, 2010) has evaluated the operating efficiency of 28 commercial banks of Pakistan over the course of five-year period, i.e., 2003-2007, by using the traditional method and Data Envelopment Analysis (DEA) approach. The results of the traditional method propose that improvement in operating income has no relationship with privatization. Furthermore the results of DEA also shows that public banks are more efficient in their operations that private banks.

In the paper (Barghandan, 2014) observe the privatization effect earlier and later than shifting of ownership. The effect noticed is on the financial performance and rate of investment returns. The data has been collected from 2000 to 2010 of the Privatized companies of Iran. The main source of data is the annual financial statements. T static is used to analyze the result. The results show that privatization has positive impact on both financial performance and rate of investment returns. Privatization leads to firm's profitability.

(Mathew Tsamenyi a, 2010) inspect the performance of two large privatized companies in Ghana. The purpose is to observe how and why these organizations have been declared to be doing well. The performances of the firms are examined from five main perspectives—financial, customers, internal business process, learning and growth, and the community. The evaluation is based on data collected from diverse sources, namely, semi-structured interviews and discussions with managers of the selected companies and with personnel from key government departments, and analysis of internal and external documents. The result shows that both companies have improved their performances after privatization which shows that privatization helps Ghana to prosper.

In the paper (Oliveros, 2012) has compared the pre privatization and post privatization performance of state-owned enterprises denationalized in Spain with the proficiency of their contiguous private opponents. The main aim of the paper was to find out whether changes in ownership structure bring revolution in the performance of the organization. The DEA approach is used to analyze the data. The results show that privatization has positive impact on privatized firm. The productivity of newly denationalized firms expressively upturns after their denationalization. The private firm has shown no such difference in its performance.

Privatization has its impact on organizations performance, many researchers has difference in their opinions. In this paper (Wang, 2011) has explored what influence does privatization has on firm's performance. The study is conducted for Chinese scenario and for the purpose 127 listed companies are used as sample of the study. Profitability and efficiency are used as main factors of the study. The results implies that transfer of ownership from government to private sector enhance the operational efficiency and financial performance of the organization which is evident that privatization has positive impact on firms performance.

In the paper (Feng, 2013) merges the stationary effect of ownership and the forceful effect of privatization on bank performance. The study is conducted in Chinese scenario so Chinese privatized banks are taken as model during from 1995 to 2010. The main reason of the study was to find the impact of privatization on returns inflow and competence gains of privatized organizations. The result shows that privatized banks are more efficient in generating returns inflow and competence gains during the given time, which shows privatization helps in effective upraise in performance.

(Ram, 2012) conducted a study to find out the relation between privatization and job satisfaction. For the purpose the data has been collected by privatized telecom company in a developing country. A total of 51 employees are used as a sample. Data has been collected through questionnaire comprising of 25 problems that were rated on a five-point Likert-type scale. The extent of job pleasure is determined by a mixture of jobs, work, and individual characteristics in this paper. The result shows that there is no direct relationship between privatization and job satisfaction in telecom sector but the result may vary sector to sector.

In the paper (Yogesh, 2012) has compared the privatized power sector of two economies namely India and Argentina. The data has been collected from the period 1991-2008. The main goal of the study was to discover how the difference in reforms affects privatization in different economies. The result shows that difference in reform has different effect on the efficiency and productivity of the firm in power sector of different countries.

3. Methodology

The study focuses on the impact of privatization on the profitability, leverage and earnings per share of the privatized banks in Pakistan.

3.1 Data sources and collection techniques:

In order to generate results we compare the financial ratios of privatized and public sector banks of Pakistan. The data for this research in order to find the profitability, leverage and earnings per share, of privatized banks (MCB and ALB) and public sector banks (NBP and FWB) quantitative data collection is taken from their financial statements. The data has been collected from the year 2009-2014. The data collected will be secondary.

3.2 Statistical technique

Software SPSS (statistical package for social science) is being used for finding descriptive statistics and graphical analysis.

Table 1 Descriptive Statistics

Ratios	Public Sector Banks		Privatized Banks	
	Mean	Std. Deviation	Mean	Std. Deviation
return on equity	5.1833	13.27083	26.9950	2.45994
return on asset	1.6808	3.60302	2.4867	.55867
capital adequacy ratio	22.2542	7.22251	18.5217	3.50415
earnings per share	3.1892	4.42738	13.9017	4.74163

4. Data Analysis

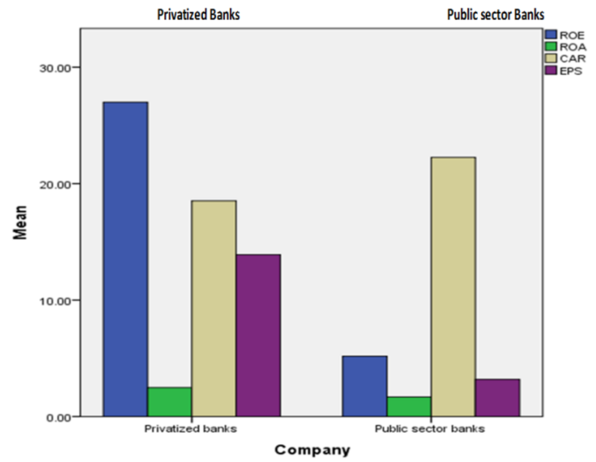
To analyze the data for this study descriptive statistics and graphical analysis is practiced. The financial statements of privatized banks (MCB and ALB) and public sector banks (NBP and FWB) are taken to verify the objectives of the research. Ratios that has been calculated for this research are

- Return on equity
- Return on asset
- Capital adequacy ratio
- Earnings per share

Descriptive Statistics

See table 1.

Graphical Analysis



The above graph shows the performance of privatized and public sector banks over the period of six years (2009-2014). This graphical representation of data shows that privatized banks are more profitable than public sector banks as the ratios of return to equity and return to asset are higher for privatized banks (ROE 26.9950 & ROA 2.4867) than public sector banks (ROE 5.1833 & ROA 1.6808). Capital adequacy ratio indicates the level to which the investment and reserves of a bank is capable to cover its liabilities. The CAR of public sector bank (CAR 22.2542) is slightly higher than privatized banks (CAR 18.5217) showing that public sector banks are less risky than privatized banks. The earnings per share of privatized bank (EPS 13.9017) is higher than public sector banks (EPS 3.1892) which indicates that privatized banks has more bright future perspective than public sector banks.

From the evaluation of three variables profitability, leverage and earning we find out that privatized banks are performing better than public sector bank. Privatized banks are more profitable and has upright outlook for future.

Conclusion

The purpose of this research was to examine the impact of privatization on bank's performance of Pakistan. To assess the performance a study was carried out by comparing privatized banks (MCB and ALB) and public sector banks (NBP and FWB). The focus was to measure the profitability, level of leverage and earnings per share of the banks during the period of 2009-2014. The results shows that privatized banks are performing superior than public sector banks as the ratios are evident that privatization has improved the overall outlook of the bank's performance. The outcome shows that privatization has positive impact on the profitability and leverage of banks. This research shows that privatization is a valuable process for the betterment of the firms and ultimately for the economy.

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