

Current Status of Public and Privatized Public Enterprises of Nepal

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Abstract

Public enterprises are established under the ownership of government. They have major objectives such as developing economic and social infrastructure, and creating employment opportunities to improve import substitution. However, they became burden to government funds in 1980s due to their inefficiency at work. In this background, adjustment program was launched in the world for improved performance of the enterprises through privatization. Nepal privatized 30 public enterprises from 1992 to 2011 under different models. The main objective of this study is to show current status of privatized and government owned public enterprises of Nepal. The analysis shows that 30 percent privatized public enterprises earned profit. The return on share capital and sales of government owned public enterprises is found higher than privatized public enterprises in the study period.

Keywords: Privatization, Public enterprises, Return on share capital, Return on sales, Sale of share

Background of the Study

After the end of the Second World War, public enterprises (PEs) were established under the ownership of government. They tailored their objectives as to stimulate economic activities in the country, develop economic and social infrastructure, distribute qualitative goods and services at fair price, create employment opportunity, help to improve import

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substitution and utilize foreign aids. Nepal's endeavor largely resembles the objectives of other countries in the world. Raut (2010) has observed, "During 1950's the private investment was not common due to the infant corporate culture and Nepal adopted inward-oriented development strategies that emphasized import substitution, industrialization and accorded to the state in the articulation to implementation of the strategy (p.3)" Sixty-three PEs are recorded to have been established in different sectors at the end of seventh national plan, *i.e.*, by 1990. After 1980, PEs were criticized as inefficient and burden to the government fund. The most common argument against state-owned enterprises pointed the inefficiency arising from state ownership due to political intervention in decision making. Samphantharak (2019) has presented four major causes of inefficiency of PEs: (1) an absence of effective ownership, (2) a lack of competition, (3) soft budget constraints, and (4) multiple objectives (p.1). Other causes include poor management, misuse of resources, poor accountability, and often huge losses to improve the efficiency of the assets invested (Kim & Panchanatham, 2019). Due to these and many other reasons, PEs had to undergo very tough times.

The Privatization Act, Nepal (1994) defined 'privatization' as involving private sector in the management of the enterprise, or to sell or lease it, or to transfer government ownership into public ownership, or an act to infuse participation by any means, either wholly or partly, or private sector or of the employees or workers, or of all desirous groups (Article 2.b). The definition emphasized ownership transfer process from government to private sectors. These objectives are not far from the objectives articulated in other countries of the world as the major aim of privatization is to change the way enterprises are managed and operated (USAID Nepal, 1996, P.6). In privatization, assets of PEs are transferred and management is handed over to private sectors. The owners have right of strategies formulation, price fixation right, and sharing profit.

The main emphasis of privatization is reduction of burden on the government funds as subsidies. The other objectives are strengthening professional competition, improving public finance, funding infrastructure development, assigning responsibility and accountability to shareholders, reducing unwanted interference, getting a committed labor force, and so on (Kim & Panchanatham, 2019, p.4). The expectation from privatization was noted by Joshi (1999) as reducing social costs and dislocations. It is clear that

ownership of public enterprises was transformed from government to private sector with the objectives of improvement in profitability and efficiency of such enterprises.

Debates in favor or against privatization of the public enterprises prevail prominently. The supporters of privatization foreground the issue of inefficiency of public enterprises, excessive control of government, lack of accountability, political intervention, etc. The study of De-Wenter and Malatesta (2001) concluded that privatization could raise the profitability of the firm. The opponents of privatization have claimed that privatization raised private monopoly and exploit publics. The studies of Gupta (2004) and Poczter (2016) concluded that public ownership is better than private ownership as private ownership have no any impact on performance. According to Parker (2004) corporate governance, transparency, accountability, shared responsibilities and ethical practices contribute to better performance.

The Government of Nepal has established 63 PEs in industrial, trading, social, public utilities, financial and service sectors. Out of them 30 are found to be privatized after 1990 till now and earned Rs. 6,435,497,000 from privatization program. The Nepal Dursanchar Company Limited holds 66.26 percent of total amount generated from privatization of public enterprises. According to Nepal Government, the last record of privatization was done in 2008. At present, the Government has 44 PEs out of which some are newly established, many are running and some are about to close.

Statement of the Problem

Economic growth is a major issue for sustainable development and prosperity of any country. For this purpose, the governments have to raise revenue and control over government cost. Different sources such as interest, dividend from investment etc. are utilized to contribute to the revenue. Mapping the operational efficiency of private as well as government owned enterprises enhance profit earning capacity. It is blamed that the operational efficiency of private sector is better than the government owned enterprises. The supporters of privatization allege that delay in decision making and government intervention for political benefits, etc. are major causes of low performance of government owned enterprises. It is argued that privatization focuses on boosting up operating efficiencies of PEs through handed them

over to private sectors as a way of sales, lease, contract management, etc.

In Nepal, 44 PEs are being operated through government ownership. Similarly, 30 privatized PEs in Nepal have 30 years' experience (Sarbjajnik Sasthanko Barsic Sthiti Samishya, 2080). In such context, the question- -- what is the operating condition of privatized and Public Enterprises of Nepal? – becomes pertinent.

Different models of privatization of public enterprises are found to have been practiced in the world. The privatization models applied in Nepal are liquidation, sale of assets, sale of shares, sale or lease of assets, and management contract. Assessing these models, Bachiller (2017) has concluded that method of privatization is a determinant of the performance of privatized companies. The companies privatized through public offering are observed to obtain a better performance than companies privatized using other methods. This observation directs us to a pertinent question: which model of privatization is suited in Nepalese context? The responses are diverse and disputed as they are presented from the perspective of political thoughts – socialism or market orientation. Another important question is: what is the current status of privatized and government owned public enterprises of Nepal?

Objectives of the Study

The major objective of this research is to assess the present operating condition of privatized and government owned public enterprises of Nepal. The objectives of this research are:

To assess the present operating status of Public and Privatized Public Enterprises of Nepal.

To analyze the models of privatization that are successful in Nepal.

To assess the current privatization situation of Nepal.

Literature Review

Restructure program of PEs started in 1980s. The history of privatization is agreed to have begun with British Government's decision to sale British Telecom, British Gas etc. Such measures in Britain as well as in other countries were due to the fact that PEs' performance declined, and they escaped away from their objectives and became government burden due to

poor financial performance. Stiglitz (1992) rightly observed that privatization entails the conversion of public enterprises formerly controlled by government to private sectors. Similar is the idea of Narain (2003) who states privatization as the role back of the state in the lives and activities of publics. In a narrow sense, it refers to the transfer of control over assets or activities through leasing where ownership is retained, leaving management of assets and activities to private sectors.

Various scholars have studied the reasons for privatization. The five forces of privatization identified by Savas (2000) include economic, populist, ideological, commercial and pragmatic. Megginson (2000) has pointed introduction of competition, promotion of increased efficiency, encouragement to foreign investment, exposure of PEs to market discipline, fosterage to wider share ownership and increase of revenue for the state. From all these understandings it can be inferred that the marathon of privatization in the world is performed to reduce government role in business activities and induce private sector for better efficiency and performance of PEs.

Privatized programs are found to play a crucial role in various aspects of enterprises. Meta regression analysis of Zahra et al. (2000) concluded that privatization through IPO plays an important role for the performance enhancement and development of the institutional infrastructure, and governance mechanisms improve the performance of PEs. The works of D'Souza et al. (2001), Von Eije and Megginson (2008) and Arcas and Bachiller (2010) and others support the finding of the meta-analysis. Hong and Park (2016) analyzed the impact of privatization in Korea using Malmquist analysis and DEA. It is found that privatization influenced the productivity of enterprises but did not contribute to their efficiency.

The studies in Nepali context have drawn various conclusions. KC (2008), who studied ten privatized PEs, observed remarkable increase in sales of three enterprises, and only two could make profit. It is concluded that privatization did not meet the objectives that the government had set. The study by Raut (2012) highlighted, "The recent experience with privatization is not so encouraging in Nepal. Although privatization process has been slowed down recently, the performance of the already privatized public enterprise has grossly suffered primarily because of labor issues, scarcity of

raw materials and long hours of load shedding (p. 16).” These studies do not show a promising contribution of privatization in Nepal.

The study of Megginson (2017) recorded \$1872.5 billion as the amount of privatization from 1988 to 2008 in the world. It was found to be \$1761.5 billion from 2008 to 2016. Estrain and Peeestier (2018) showed privatization revenue less than \$50 billion in Africa, Middle East and South Asia each, about \$220 billion in Latin America from 1988 to 2008, and \$ 17.45 billion in South Asia. In South Asia, India has run limited privatization program, and China has run corporatization of PEs.

Mandiratta and Bhalla (2017) evaluated disinvestment performance pre and post period of privatization of partial share sales through either IPO or FPO public enterprises. Taking 15 privatized CPSEs panel data from 2002 to 2012 and analyzing with the help of financial ratios and Wilcoxon signed-rank test. It is concluded that there is a positive impact on operating performance (sales revenue) but not in profitability. They have given government intervention on decision making and policy formulation as the reasons of low profitability.

Phi et al. (2019) report on the performance of state owned enterprises and private owned enterprise profitability and leverage found evidences of outperform of state owned enterprises in comparison to their counter private owned enterprises. State owned enterprises supplied goods and services without profit maximization behavior, and they were more dependent on debt and financial support than share capital. The state owned enterprises were costlier due to more labor incentive than private owned enterprises. They also suggested that privatization could motivate public and private enterprises to encourage state owned enterprises to shift their management toward maximize profitability and efficiency policy.

Borbovic and Tabak (2020) studied economic performance of state owned enterprises (SOE) in emerging economy of 25 countries with the data from 2014 to 2016. They concluded SOEs are powerful in many countries. The SOEs were increasing in Hungary, Turkey and Poland. The planned privatization program of many countries was found slow or delayed. The study recommended that there are opportunities in many countries to improve operational efficiencies of SOEs and upgrading the corporate governance.

Research Methodology

This research is descriptive and analytical. Secondary data from all the privatized and government owned PEs are taken as population and sample. The financial data available from privatized and government owned public enterprise since 2015/016 to 2018/019 are used. Financial data are taken for financial performance analysis and number of privatized public enterprises for analysis of successful model of privatization. The percentage and return on share capital and sales revenue ratio are calculated. The data is taken from government publication and other research articles from internet.

Results

The Nepal Government launched Privatized program in 1992 and the program is still continuing. The following table summarizes the government's privatization activities:

Table 1: *Period wise Privatized Public Enterprises*

Year	No of Privatized Enterprises	Percentage
1992-1996	12	40
1997-2001	3	10
2002-2006	14	46.67
2007-2011	1	3.33
2012-2016	-	-
2017-2021	-	-
Total	30	100

Source: Annual performance review of Public Enterprises, 2077

Table 1 shows the total number of privatized PEs and their period of privatization. The period of 1992-1996 and 2002-2006 privatized 86.67 percent of the enterprises. The last privatized PE was Dursanchar Company Limited under the model of share issue in 2011.

Sector-wise Public Enterprises

PEs in Nepal are classified under six sectors – Industrial, Public Utility, Trading, Financial, Social, and Service. The table below (Table 2) presents sector-wise figure of PEs operating from 2007/008 to 2020/2021:

Table 2: *Sector-wise Public Enterprises in Nepal*

Sector	Number 2007/008	Number 2020/2021	% increase or decrease
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Industrial	7	10	42.85
Public Utility	3	5	66.67
Trading	6	5	-16.67
Financial	8	9	12.15
Social	5	5	0
Service	7	10	42.85
Total	36	44	22.22

Source: Annual Performance Review of PEs from 2009 to 2021.

Table 2 shows six sectors of PEs operating from 2007/008 to 2020/021. The Government has increased 22.22 percent PEs from 2007/008 to 2020/021. In this period, the government sold the share of Door Sanchar in 2011. The maximum number is found to have increased in Public Utility by 66.67 percent.

Investment on Public Enterprises by Nepal Government

The table below (Table) 3 shows the total investment made by Nepal Government on PEs as shares capital and loan.

Table 3: *The Share and Loan Investment in Public Enterprises by Government* (in Billion)

Investment	2007/008	2020/021	%
Share Capital	81.92	271.83	331.82
Loan	73.81	192.75	261.14
Total	155.73	464.59	298.33

Source: Annual performance Review of PEs 2009 to 2021.

The share capital and loan investment on PEs' is found to have increased notably after 2007/008; it increased by 298.33 percent.

Model of Privatization, Operating Condition, and Profit and Loss

The privatization model helps to analyze preferable model analysis of privatization.

Table: 4: *Privatization Models, Present Condition and Profit and Loss*

Methods	Privatized	Present	Profit or loss
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	PEs		Condition	No		Profit		Loss	
	No	%		No	%	No	%	No	%
Liquidation	12	40	Closed	12	40				
Assets and business sale	3	10	Closed	3	10				
Sale of Share	11	36.67	Closed	3	10				
			Operating	8	26.67	8	26.67		
Assets sold on lease	3	10	Operating	3	10	1	3.33	2	6.67
Management contract	1	3.33	Operating	1	3.33			1	3.33

Source: Annual performance review of Public Enterprises, 2079

Table 4 shows that 50 percent PEs were either liquidated or assets and business sold. The remaining 50 percent were privatized under the model of sale of shares, assets sold on lease, and management contract. The sale of share were found more successful; and out of 11 such PEs eight are in operation and earned profit. The sale of assets on lease were found in operation but not successful in earning profit.

Financial Performance Analysis

The comparative financial performance of privatized public enterprises and public enterprises on the basis of return on sales and return on equity share capital is shown in Table 5.

Table 5: *Financial Performance Analysis PPEs and Public Enterprises (PEs)*
-RS. In Million

Head	2015/016	2016/017	2017/018	2018/019
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s	PPEs	PEs	PPEs	PEs	PPEs	PEs	PPEs	PEs
Share Capital	2111.7	14358.6	2260.4	18277.4	2637.8	22207.9	2963.8	28550.4
Sales revenue	2270.0	24050.2	2989.4	32206.9	3205.0	39082.5	6092.2	47026.2
Net Profit	304.6	34960.9	344.8	41427.7	357.2	43448.7	327.8	48774.8
Return on sales	13.41	14.54	11.53	12.86	11.14	11.12	5.38	10.37
Return on Share Capital	14.42	24.35	15.25	22.67	13.54	19.56	11.06	17.08

Source: Annual Performance Report, Report of PEs from 2015/016 to /2020/2021

As shown in table 5, investment in share capital and sales revenue are found to be in increasing trend in privatized and existing PEs. The return on sales and return on equity shares are found to be in decreasing trend. The ratio of return on sales of privatized PEs show 13.41 in FY 2015/016, which decreased to 5.38 in FY 2019/020. The return on share capital was 14.42 in 2015/016 and 11.06 in 2019/020. The return on sales ratio of existing PEs was 14.54 in FY 2015/016 and 10.37 in 2019/020. The return on share capital was 24.35 in 2015/016, which decreased to 17.08 percent in FY 2019/020. Both ratios of privatized and existing privatized PEs showed decreasing trend of operating performance. The lower ratio of privatized public enterprises than existing PEs means weaker operating performance of pprivatized PEs.

Discussion

The objectives of PEs establishment have been massaged as a Pandora box in

the world. It is taken as a means of crisis management, economic strengthening, vehicle of development and social equity etc. In 1980s, it was realized as a burden to government funds, and thus structural adjustment program were lunched in the world. The British Telecommunication was a pioneer of privatization program in the world. In 1990s, privatization was faster and done worldwide to transfer ownership of enterprises from government to private sector for enhancing operational performances, increasing investment and providing funds to government for operating activities.

Nepal lunched privatization program with the sale of Bhrikuti Paper and Pulps Mill 1992 though Privatization Act was sanctioned in 1994. The Nepal Government privatized 30 public enterprises from 1992 to 2011. During this span, privatization was intensive in the period of 1992-1996 and 2002-2006. In both these periods, Nepali Congress Government ruled mostly . The latest attempt of Government of Nepal was to privatize Nepal Airline, which shows that there is a thirst of privatization. The Government has increased share investment by 331.82 percent from 2007/008 to 2019/020. The Government has invested on Vidhyut Utpadan Company, Dhaubadi Falam Company Ltd Ltd., Hydroelectricity Investment and Development Company Ltd., Nepal Railway Company, Nepal Infrastructure Company Ltd, etc. There has been different causes of delay in privatization such as lack of political commitment, unstable government, problems of ideological reconciliation between different political parties and socialism oriented constitution etc. From all this present status of privatization, it can be inferred that the process is in coma. Raut (2012) also agrees on slow movement of privatization program of Nepal. This inference resembles the findings in Hungary, Turkey, and Poland. The planned privatization program of many countries have been found slow or delayed in the study period (Borbovic and Tabak (2020).

Among the privatized PEs only 30 percent are successful to run business and earn profit from the sale of share model. The model of liquidation and sales of business are not in existence in business activities. Assets sold in lease have been found at loss. Among the methods, sale of share is partially successful in Nepalese context. This observation resembles the study of Zahra, et. al. (2000), Von Eije and Megginson (2008) and Bachiller (2010). The reason behind failure of assets sold and liquidation are: defect in

valuation process of privatization, more benefit to investor in alternative work, weak monitoring system after privatization, weakness in rules and regulation, and poor management, etc. Sale of share, which is public private investment method, is found more successful in Nepal.

The operating performance on the basis of return on sales and share capital of privatized public enterprises are found lower than government owned public enterprises. The amount of share capital and sales are observed to have increased in study period, but the profit has declined year by year. The reason may be increased competition at market, low scale of production and sales, high labor cost, problems of technology friendly environment, etc. This observation resembles the study of KC (2008), Raut (2012), Hong and Park (2016).

Conclusions

Following the launch of privatization program in 1992, Government of Nepal has privatized about 50 percent public enterprises through different models. Among the various models, the sale of share model is more successful than other models such as the sale of assets and business, assets sales in lease, management contract and liquidation. The fact that Nepal Government is unable to privatize any public enterprises after 2011, but continued establishing new public enterprises with additional capital investment is a serious concern. The operational performance has not been found to be satisfactory. The investment sales has increased with decreasing trend of profit. The expectation of improvement in the performance of privatized enterprises has been found wrong. Hence, it becomes imperative for the government to find the causes of failure in operation of Privatized PEs. It should emphasize accountable, responsible management and maintain good corporate governance in the Privatized PEs. Similarly, it should provide planning authority, and decision making role to management for developing professionalism. Further studies examining the declining number of privatized PEs should uncover many other facets of the privatization program.

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