

AN EVALUATION OF THE FINANCIAL PERFORMANCE OF PUBLIC SECTOR UNDERTAKINGS IN KERALA

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Abstract

Public enterprises are those enterprises in which the government holds at least 51 per cent of the shares of the company. Financial performance assesses the strengths and weaknesses of the company by assessing financial items present in the consolidated financial statements. The study utilized secondary data, primarily from official documents published by the Kerala government, and ratio analysis was employed as a tool for evaluating various financial indicators of the companies. The study was carried out from 2017-18 to 2021-22. The research design is descriptive and analytical in nature. The operating efficiency fluctuates throughout the study, and the liquidity position is improving. The study also found that the companies had an inconsistent financial structure. The study concludes that the overall profitability of the companies was poor.

Keywords:- Public Sector Undertakings, Financial Performance, Ratio Analysis, Liquidity, Profitability, Operating Efficiency, and Solvency.

*I*n a rapidly changing world, different forms of business exist (Yameen & Pervez, 2016). Public Enterprises are those organisations that are owned, controlled and operated by the government at various levels (international, national, or local)(He et al., 2021; Mitra & Pol, 2019). PEs offer services to the public at a

reasonable price (Mitra & Pol, 2019). The majority of the investments of these companies are made by the government (Mitra & Pol, 2019). The main objectives of state-owned enterprises are related to improving social conditions and political interests, including price stability, employment promotion, and an increase in the values of

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assets and foreign exchange reserves(He et al., 2021).

Financial performance evaluation helps to identify the strengths and weaknesses of the company by assessing the different financial indicators of the company, and also determining the financial health of the company(Yameen & Pervez, 2016). It reveals the performance of the financial activities in the organization(Ahmad, 2016). The financial performance of PSUs has remained very low, due to high interest rates, poor asset utilisation, and operational inefficiency (Mitra & Pol, 2019). If a company achieves sound financial performance, it indicates that the firm has attained profitability, market share, and a competitive advantage, which are essential for its survival(Yameen & Pervez, 2016). It holds a prominent place in the state's economy and the welfare of its people. Kerala has 131 PSUs after merging, transferring, liquidating, and closing units. The majority of PSUs are facing losses, so the government must take the required actions to improve the companies' profitability(Bureau of Public Enterprises, 2023). The research paper focuses on the performance of the liquidity, solvency, profitability, and operating efficiency of the PSUs in Kerala and how it benefits to the stakeholders. The study gives an overall idea about the PSUs' financial performance and also provides suggestions for improvement.

Review of Literature

According to He et al. (2021), the overall financial performance of both public and private companies was low after analysis of the selected financial

indicators. Abramov et al. (2017), the performance of private companies was better than that of public companies in Russia. The study concluded that government ownership negatively influenced the profitability (financial performance) of the companies, whereas there was a positive influence between government ownership and debt burden. Yameen & Pervez (2016) says that the selected company's liquidity, management efficiency, market valuation, and profitability were deteriorating during the study. The study revealed that the overall financial performance of the company declined during the study.(Mitra & Pol, 2019), the researchers found that the asset turnover ratio and net profit margin played an important role in generating a positive return on equity, but the financial leverage was an irrelevant factor in generating a return on equity identified with the help of panel regression analysis. (Ahmad, 2016)used multiple regression analysis to determine that liquidity, solvency, and efficiency ratios did not affect the return on capital employed. The financial performance of the company was poor.

Research Gap

Many research studies are based on the financial performance of private firms as well as public companies at international and national levels. However, the paper related to the overview of the financial performance of the company is limited. It is important to study the financial performance of PSUs in Kerala to give awareness to the government and society about profitability, liquidity, solvency and operating efficiency.

Statement of the Problem

Public Sector Undertakings (PSUs), both at the Central and State levels, play a significant role in the growth and development of the country. The financial performance of the public enterprises of Kerala is evaluated by examining their liquidity, solvency, profitability, and operating efficiency. If the financial performance of PSUs is not up to standard, then it will affect the economy of our country. The study gives direction to the state government to look after loss-making PSUs in Kerala and also raise awareness among other stakeholders about the present condition.

Many of these enterprises have been facing serious financial challenges, such as facing losses, liquidity and solvency constraints, and declining operational efficiency. Without such analysis, policymakers and stakeholders cannot make informed decisions regarding restructuring, revival, or closure of loss-making units.

Objectives

- 1) To analyze the liquidity and solvency of the Public Sector Undertakings in Kerala.
- 2) To evaluate the profitability and operating efficiency of the Public Sector Undertakings in Kerala.

Research Methodology

The research design is descriptive and analytical in nature. The study utilized secondary data to comprehend the financial performance of the Public Sector Undertakings in Kerala. The census method is used in the study. The

consolidated financial data of 131 PSUs was obtained from 'A Review of Public Enterprises in Kerala 2021-22', 'A Review of Public Enterprises in Kerala 2020-21', and 'A Review of Public Enterprises in Kerala 2019-20' published by the Government of Kerala. Ratio analysis is employed in this study to evaluate the company's financial position. The study was carried out from 2017-18 to 2021-22 for a period of five years. Ratios are calculated based on the information obtained from secondary sources.

Scope of the Study

The study was conducted to analyze the financial performance of Public Sector Undertakings in Kerala over five years from 2017-18 to 2021-22 with the help of ratio analysis. The study concentrated on the financial aspect of PSUs in Kerala only. The study provides an overview of the liquidity, solvency, operating efficiency, and profitability of the PSUs in Kerala.

Significance of the Study

PSUs play a significant role in the economic growth of the country, provide employment for the youth, provide goods and services for the people at a reasonable price, provide financial aid for strategic industries, and offer other benefits to the people of our country

The study helps to understand the current financial performance of PSUs in Kerala. If the financial performance of PSUs is good, their benefits will go to the stakeholders. The government should frame a policy to enhance the profitability, liquidity, solvency, and operating efficiency of the PSUs in Kerala. It will help the

managers of the PSUs to improve the resource utilisation, cost control and financial planning. If the PSUs shut down, it will affect all the stakeholders of the company, including the public, employees, managers, creditors, shareholders, and suppliers. The study raises awareness in society and the government to enhance the profitability of PSUs; otherwise, many PSUs will lead to bankruptcy.

Data Analysis

Current ratio

The current ratio measures the relationship between current assets and current liabilities. Current ratio = Current assets / Current Liabilities.

The average current ratio of PSUs in Kerala is 1.386, indicating that the short-term solvency of the PSUs is satisfactory, but it also displayed a low standard

deviation, implying that the current ratio of PSUs did not change smoothly. The current ratio of PSUs in Kerala has increased over time, indicating that the short-term solvency situation has improved. The current ratio increased steadily from 1.129 in 2017-18 to 1.515 in 2021-22. This ratio indicates a company’s ability to meet its short-term obligations with its current assets and suggests an improving liquidity position over the year. The mean current ratio of 1.386 over the five years indicates the organization could meet its short-term liabilities, while the standard deviation of 0.1742 shows relatively low variability in the current ratio.

Debt – Equity Ratio

The debt-equity ratio is the key financial metric that measures the company’s proportion of debt financing

Liquidity Position

Table 1

Liquidity Position of PSUs in Kerala

	2017-18	2018-19	2019-20	2020-21	2021-22	Mean	S.D.
Current ratio	1.129	1.27	1.44	1.46	1.515	1.386	0.1742

Source: A Review of Public Enterprises in Kerala.

Solvency Position

Table 2

Solvency Position of PSUs in Kerala

	2017-18	2018-19	2019-20	2020-21	2021-22	Mean	S.D.
Debt-equity ratio	10.78	-13.58	-11.27	-5.512	5.07	-2.90	10.50

Source: A Review of Public Enterprises in Kerala

Profitability Position

Table 3
Profitability Position of PSUs in Kerala

	2017-18	2018-19	2019-20	2020-21	2021-22	Mean	S.D.
Net profit ratio (%)	-9.57	-2.76	-4.91	-10.86	-4.6	-6.54	3.48
Return on net worth (%)	-13.4	-15.86	- 21.4	-19.65	-10.019	-16.07	4.60
Return on Capital employed (%)	-7.69	-2.8	-4.69	-9.427	-3.708	-5.66	2.79

Source: A Review of Public Enterprises in Kerala

relative to equity financing. Debt – Equity Ratio = Debt / Equity

The mean value of the debt-equity ratio reflects that the company does not have enough equity to offset the debt taken from the government. The high standard deviation of the debt-equity ratio represents the inconsistent financial structure of the companies.

Net Profit Ratio

The net profit ratio shows the relationship between net profit after tax and interest and net sales.

Net profit ratio = Net profit after tax and interest / Net Sales

The net profit ratio remained negative from -9.57 in 2017 -18 to -4.6 in 2021-22, indicating consistent losses of PSUs during the study period with some fluctuation in profitability.

Return on Net Worth (RONW)

Return on Net Worth or Return on Shareholders’ funds measures the profitability of a company relative to the shareholders’ equity(Ahmad, 2016).

Return on Net Worth (RONW) = Net profit after tax and interest/ shareholders’ equity x 100

Return on Net Worth ratio is also consistently negative, showing an inability to generate a return on equity. The mean Return on Net Worth ratio is -16.07 per cent, with the highest variability among the three metrics. Negative values indicate that the PSUs in Kerala are eroding the shareholder value. RONW remains negative across all years, with the lowest value of -21.4 per cent in 2019-20 and the least negative value in 2021-22 is 10.019 per cent. The PSU’s equity is not generating any returns but is declining in value identified with the help of mean and standard deviation. The mean RONW is -16.07 per cent representing the equity erosion over time, while the standard deviation reflects high variability due to inconsistent equity levels.

Return on Capital Employed

Return on Capital Employed (ROCE) shows the relationship between the net profit before interest, tax, and dividend, and net capital employed(Ahmad, 2016). Return on Capital Employed (ROCE) = Net profit before interest, tax, and dividend / Net capital employed x 100

Return on Capital Employed (ROCE) also remains negative, ranging

from -2.8 per cent in 2018-19 to - 9.427 per cent in 2020-21, with a mean of - 5.66 per cent. The negative ROCE implies that both debt and equity capital are not being employed in the organizations effectively to generate a positive return, and also inefficiencies or issues in managing investments. The variability in ROE was found from the standard deviation of 2.49. The profitability of public sector undertakings in Kerala fluctuated during the period. The loss of PSUs dropped in the early years but increased following the decrease in 2021-22. The Public Sector Undertakings in Kerala faced a loss in the initial years, but they tried to overcome the situation. However, the situation worsened following the pandemic, and they attempted to overcome it. The net profit ratio, return on net worth, and return on capital employed were all negative. The profitability of PSUs was negative during the period, and the overall performance of the public sector undertakings in Kerala was not satisfactory. According to the study, our state has more loss-making PSUs than profit-making ones. Some PSUs were focused on earning profit. PSUs operate in the state to offer services rather than for profit.

Turnover to Capital Employed Ratio (Capital Turnover Ratio)

The turnover to capital employed ratio shows the relationship between sales and capital employed. $\text{Turnover to capital employed ratio} = \text{Net Sales} / \text{Capital employed}$. Turnover to capital employed ratio varies from 0.80 to 1.02 over the five years, with a mean of 0.8861 and a standard deviation of 0.1007. The turnover-to-capital employed ratio is relatively stable, with a slight decline over the five years. It shows consistency in the value, but gradually decreases the efficiency of the company in using the capital of the company to generate turnover. The standard deviation of the turnover to capital employed ratio is low, indicating that there is consistency in the ratio, but the ratio of operating efficiency has declined in the last two years, which might imply potential operational challenges or increased capital without a proportionate increase in revenue (Bureau of Public Enterprises, 2023).

Total Assets Turnover Ratio

The total assets turnover ratio shows the relationship between net sales and total assets.

Operating Efficiency Position

Table 4

Operating Efficiency Position of PSUs in Kerala

	2017-18	2018-19	2019-20	2020-21	2021-22	Mean	S.D.
Turnover to capital employed ratio	0.80	1.02	0.96	0.86	0.7905	0.8861	0.1007
Total assets turnover ratio	0.301	0.297	0.297	0.249	0.244	0.2776	0.0284
Working capital turnover ratio	5.47	2.65	1.85	1.44	1.292	2.5404	1.720

Source: A Review of Public Enterprises in Kerala

Total assets turnover ratio =
 $\text{Net Sales} / \text{Total assets}$

The total assets turnover ratio assesses the company's efficiency in generating revenue from its total assets. The ratio remained relatively stable from 2017-18 to 2019-20 but dropped in 2020-21. This ratio reveals minimal variation over the years, and the gradual decline suggests decreasing asset utilization.

Working Capital Turnover Ratio

The working capital turnover ratio indicates how efficiently a company uses its working capital to generate sales.

Working capital turnover ratio =
 $\text{Net Sales} / \text{Net Working Capital}$

The working capital turnover ratio shows a steep decline from 5.47 in 2017-18 to 1.292 in 2021-22. The sharp drop over the years suggests an increasing inefficiency in managing working capital. The standard deviation of 1.720 represents significant variation. The operational efficiency of the PSUs was boosted and then lowered. The turnover to capital employed ratio, total assets turnover ratio, and working capital turnover ratio were used to assess the efficiency of all the public sector enterprises in Kerala.

Findings

- The current ratio indicates improved liquidity over the five years, which shows better management of current assets or a reduction in current liabilities.
- The companies do not have enough equity to offset the debt taken from

the government and the inconsistent financial structure of the companies owned by the government.

- The profitability of public sector undertakings in Kerala is low. Some businesses face closure concerns, while others operate because they give services and jobs to young people. The RONW ratio shows a negative trend throughout the study, indicating the PSUs are eroding shareholders' value. ROCE shows a negative value throughout the study, signaling inefficient use of total capital.
- The organizations are generating less revenue per unit of capital employed, signaling a gradual decrease in operating efficiency. The assets of PSUs are underutilized may be due to idle or underperforming resources, outdated technology, and inefficient working capital management impacting the capacity to generate the revenue.

Suggestions

- The government must take prompt action to decrease losses in the state companies. Some public enterprises are producing profit from the business, some public enterprises are making losses, and a few public enterprises are getting recently started.
- The management needed to make various decisions to reduce the loss of the enterprises and enhance the different financial aspects of the companies.

- The companies controlled by the government should maintain a consistent financial structure.
- The companies should monitor many financial indicators to improve their performance.
- The management needs to minimize operational inefficiencies and reduce fixed costs to improve profit and boost turnover. The PSUs need to prioritize investment in high-yield projects or operations.
- The restructuring of capital structure to maintain reasonable returns on capital employed, put forward the strategies to enhance NPR and RONW, and boost the equity return.

Conclusion

Public sector undertakings in Kerala are those enterprises that work in different sectors of the economy. The profitability position of PSUs in Kerala was not favorable, as most of the PSUs faced risks of making losses that affected the entire state. The liquidity position was satisfactory but operating efficiency fluctuated throughout the study and solvency was not favourable, which represents the inconsistent financial structure of the companies. The companies need to take necessary steps to improve the financial performance of the PSUs in Kerala.

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