ISSN : 1412-0437

FORDEMA

(FORUM DOSEN EKONOMI MANAJEMEN dan AKUNTANSI)

Volume 8 Nomor 2, November 2008

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LEMBAGA PENERBIT FAKULTAS EKONOMI
UNIVERSITAS MUHAMMADIYAH PALEMBANG

FORDEMA | VOL. 8 | NO. 2 | PALEMBANG NOVEMBER 2008 | ISSN 1412-0437

FORDEMA

(Forum Dosen Ekonomi Manajemen dan Akuntansi)
Volume 8 Nomor 2, November 2008

FORDEMA diterbitkan sejak 2001, dengan frekuensi 2 kali setahun.
Redaksi menerima karangan ilmiah tentang hasil-hasil penelitian,
Survey, dan telaah pustaka yang erat hubungannya dengan bidang Ekonomi.

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Pengantar Redaksi

Pembaca Fordema yang terhormat,

Assalamu'alaikum Wr. Wb.

Alhamdulillah, Puji syukur kehadirat Allah SWT atas nikmat yang telah diberikan kepada kita semua sehingga Jurnal FORDEMA dapat kembali hadir ditengah-tengah pembaca.

Pada edisi ini, Fordema menyajikan beberapa artikel baik penelitian dan non penelitian di bidang manajemen dan studi pembangunan , seperti : **Isnurhadi** ,tentang, Determinants Of Operating Performance Of Malaysian State Owned Enterprises After Privatization, **Bambang Widagdo dan Sugiarti**, tentang, Model Pemberdayaan Keluarga Miskin di Wilayah Sub Urban Dalam Perspektif Gender, **Hatta Wazol** tentang Pengaruh PDRB,Jumlah Penduduk dan Jumlah Kunjungan Pasien Terhadap Penerimaan Retribusi Pelayanan Kesehatan (Suatu Kasus Pada Dinas Kesehatan Prov. Sumatera Selatan) **R. Mulyo Hendarto dan Hastarini Dwi Atmanti** Kajian Terhadap Pembentukan Daerah Otonom Baru dan Ibu Kota Daerah **Purwadi** Hubungan Pendidikan Dan Pelatihan Serta Kompensasi Terhadap Kinerja Anggota Satuan Polisi Pamong Praja Kota Palembang, **Didik Susetyo** tentang, Analisis Dana Alokasi Umum Dan Upaya Fiskal Kota Palembang

Dalam bidang Akuntansi menyajikan hasil penelitian **Dian Putri Maharani dan Sa'adah, tentang** Praktik Akuntansi Pada Perusahaan Skala Menengah Di Kota Palembang, **Welly** tentang Penghargaan, Perilaku Pimpinan, Perilaku Tim Kerja, Komitmen Organisasi, Efesiensi Perubahaan Dan Orientasi Kerjasama Terhadap Komitmen Program Serta Pengaruhnya Terhadap Kinerja Pimpinan, **Sapta Dyah Puspitarini dan Antariksa Budileksmana** tentang Pengaruh *Corporate Social Responsibility* Terhadap Nilai Perusahaan Dengan Kepemilikan Manajemen Dan Tipe Industri Sebagai Variabel Pemoderasi **Karyanti dan Suryo Pratolo,** tentang Pengaruh Kualitas Auditor, Kondisi Keuangan Perusahaan, Opini Audit Tahun Sebelumnya, Pertumbuhan Perusahaan Dan *Debt Default* Terhadap Kemungkinan Penerimaan Opini Audit *Going Concern.*

Tiada gading yang tak retak, berbagai kritik dan saran yang membangun selalu kami harapkan. Terima kasih dan semoga artikel-artikel ini bermanfaat bagi pembaca semua.
Wassalamu'alaikum Wr. Wb

Palembang, November 2008

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DETERMINANTS OF OPERATING PERFORMANCE OF MALAYSIAN STATE-OWNED ENTERPRISES AFTER PRIVATIZATION

Isnurhadi[1]

Abstract

Privatization is the transferring of ownership from state to private ownership expecting that the lackluster and unsatisfactory performance of state-owned enterprises can be improved. This study focuses on the evaluation of operating performances of the newly privatized firms which issued shares in capital market. The research was carried out by investigating the operating performance of the privatized firms after privatization and factors that are responsible on the post-privatization performance. The performance were studied through statistical analysis of the dependency of several independent variables namely performance proxies i.e. soft budget constraint, fraction of share sold, share allocated to employee and top management team change on dependent variables i.e. return on sales (ROS), return on assets_(ROA) and return on equity (ROE), real sale and net income. The results showed that the factors that are responsible on the post-privatization performance differ depending on the performance proxies. The factors responsible for ROS are the short-term debt to total asset and the share allocated to employee, the fraction of share sold and the share allocated to employee are responsible for ROA, while the ROE is affected by the top management team change only. The real sale is influenced by the fraction of share sold and the share allocated to employee, while net profit is not affected by any factor considered in this study.

Keywords: Privatization, State-Owned Enterprises

Privatization as a policy of transferring ownership from state to private or public assets has been one of the most popular economic policy for the last twenty five years. Margaret Thatcher's conservative government which came to rule United Kingdom in 1979 is regarded as the pioneer of the modern privatization programs. The policy has been adopted by many countries in which governments from various political backgrounds enthusiastically sold state-owned enterprises (SOEs, hereafter) to private investors expecting a significant improvement of the companies. This privatization policy has transformed the role of the state in the economy in almost every country in every continent from industrialized nations such as the United Kingdom, France, United States, and Japan to emerging countries such as Malaysia, Thailand, Indonesia, and Philippine in Asia, as well as Chile, Brazil, and Mexico in Latin America.

Malaysia as one of the leading economy from emerging market has embrace privatization since early 1980. The generally lackluster performance and unsatisfactory of state-owned enterprises together with economic crisis in the form of recession required the change in the policy. The then Malaysia Prime Minister Mahathir Mohamad first announced his government's privatization policy in 1983. Issuing shares in capital market is one popular mode of privatization in Malaysia which usually

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involves very large companies such as Malaysia Airlines, Telekom Malaysia, TV3, and Proton amongst others. These companies play very important role in Bursa Malaysia after privatization (Jomo, 1995).

Now after more than two decades of privatization policy in many countries in the world, the impacts of the policy have been a fertile ground to study. Privatization studies from western countries primarily western and eastern European countries are quite extensive but quite few come from emerging country like Malaysia. For example, Galal, Jones, Tandon and Vogelsang (1994) using case study approach reported an average net welfare gains in 11 of 12 privatized companies considered in their study which equal on average 26 percent as compared to the sales of the firm before privatized. Using large sample from many countries and many industries, Megginson, Nash and van Randenborgh (1994), Boubakri and Cosset (1998), and D'Sousa and Megginson (1999) report that on average the performance of SOEs is improving upon privatization. On the other hand, Harper (2001), using a sample of Czech firms, reports that the efficiency and the profitability of the firms decrease immediately following privatization.

Eckel, Eckel and Singal (1997) reports that the performance of the British Airlines improves upon privatization. Ramamurti (1997) and La Porta and Lopez-de-Silanes (1999), using a single industry sample, also report a favorable performance upon privatization. On the other hand, Martin and Parker (1995) find that only less than half British firms they studied perform better after being privatized. Newberry and Pollit (1997) conclude that British Electricity Company's (CEGB) restructuring and privatization was in fact worthwhile, however, it could have been better implemented taking into account of public's welfare. Privatization program in some transition countries, primarily Russia is considered failed (Nellis, 1999). Privatization through mass and rapid schemes as in these transition economies of former Soviet Union and Central Easter European countries turned over assets to people who are lacking incentives, skills, and resources to manage the firm. In this institutional vacuum, privatization can and has led to stagnation rather than to better financial results and increased efficiency.

Privatization emulates debates because theoretically it is a good policy to improve the firm performance which is lacking under state ownership. However, empirical evidences show mixed results. This indicates that evidences are inconclusive and therefore more researches on privatization are warranted and more empirical results are need to better understand and explain the privatization phenomenon.

The aim of this study is to examine the effect of privatization on the financial and operating performances of state owned enterprises (SOE) and to evaluate the determinants that possibly responsible for the variation on the performance. This study contributes in many aspects. Firstly, this study employs a single country data which is more homogeneous that lead to more meaningful conclusion. Secondly, this study focuses on a soft budget constraint theory introduced by Kornai (1980) which is used to assess the phenomenon of unsatisfactory performances of many state-owned companies in formerly planned economies of Eastern European Countries.

Theory Related to Privatization

Criticism of the existence of state-owned enterprises (SOEs) is based on theories. Prominent theories that support privatization are notably property right, public choice and soft budget constraints. From point of view of property rights literatures, when a company has no clear residual claimant, no individual or group with a clearly specified right to claim any residual benefits or surplus left after other claims are met, the company will be less efficient (Alchian & Demsetz, 1972; Demsetz, 1988 and Grossman & Hart, 1986). Since no one clearly benefit from SOE's efficient operation, no one will be strongly motivated to hold management accountable for performance, hence agency problems will not be reduced. Thus, the property right analysis of public ownership leads to the conclusion that public enterprises are less economically efficient than private enterprises.

Other school of thought that shares a view of weaknesses of public ownership is public choice theory. This theory suggests that public managers, bureaucrats and politicians will use their control of SOEs to pursue their own interest, rather than the state firm's efficiency (Niskanen, 1971). Privatization allows profit-maximizing entrepreneurs to take the place of size-maximizing-bureaucrats and vote-maximizing politicians. Under public ownership which leads to large subsidies and other concessions, it is more worthwhile to lobby minister and key public official for fund than the diligent search for ways of reducing costs. Privatization frees enterprises from the burden of political inference and non-market criteria, limits politicians' ability to redirect the enterprise's activities in a way that promote their personal agenda, clarifies the objectives of the enterprise, and lead to enhanced economic performance.

The soft budget constraints theory (Kornai, 1980) argues that distortions in both the objective function that managers seek to maximize and the constraints they face is due to the so-called soft budget constraints problem (Kornai, 1980). Public managers, who tend to report to a politician and pursue their political careers, incorporate to the objective function aspects related to maximization of employment at the cost of efficiency, and political prestige (the empire building hypothesis). The reason why managers are able to do that without facing the threat of bankruptcy is related to the second distortion, the soft budget constraint. In any situation in which the firms have engaged in unwise investments, it will be in the interest of the government to bail the firm out using the public budget. The rational for this relies on the fact that the bankruptcy of the firm would have a high political cost, whose burden would be distributed within a well-defined political group, like unions. On the other hand, the cost of the bailout can be spread over the taxpayers, a less organized, larger group in society, with diversified interests and preferences. The threat of bankruptcy is non-credible under public ownership because the political loss involved in closing a publicly owned company is larger than the political cost of using taxpayer money to bail it out which results in lower efficiency under public ownership. This is the essence of this research that is to apply the soft budget constraints to assess the privatization program in Malaysia.

Methodology Research

The subject of this research is state-owned enterprises privatized through public offering in Bursa Malaysia. The sample represents the whole population of privatized SOEs that are fully and partially privatized through share issue privatization (SIP). Choosing this sample is not without reason. The firms that are privatized in this way continue to generate post-issue financial and accounting data that are directly comparable to pre-divestiture data. There are 41 state-owned enterprises listing their stocks on the Main Board of Bursa Malaysia. These firms were privatized from 1983 to 2001. However, due to the uncompleteness of the data, only 30 firms are managed to include in the sample.

Data were collected from various sources, mostly from Bursa Malaysia library, such as, stock issue prospectuses, Annual Companies' Handbooks, KLSE on disk, and individual annual company report. Other data are collected from internet sources such as, Bursa Malaysia website (http://www.bursamalaysia.com) and individual companies' websites. Part of the data on daily stock price is procured from a commercial data company i.e. Pusat Komputer Profesional in Kuantan, Pahang and some old and rare stock price data have to be taken out manually from stock daily diaries in Bursa Malaysia. Other data such as financial statement data are supplemented by Dataquest, a commercial data provider and investment consultant in Pulau Pinang.

To investigate factors that could explain the variation in firms' performance due to privatization, five models (a set of independent variable regressed on five different dependent variables) are developed. Based on the previous studies, the relationships between the dependent variables comprising of the performance proxies and the independent variables are linear in parameters. Hence, the models take the form of multivariate linear regression. The dependent variables consist of ROS, ROA, ROE, real output (RS) and real net income (NI) while the independent variables are STDA, LTDA, SOLD, EMPL and TOPMGT.

The independent variables are regressed on these performance measures and form multivariate regression models as follows:

$$P = \alpha - \beta_1 SDTA - \beta_2 LDTA + \beta_3 SOLD + \beta_4\ EMPL + \beta_5\ TOPMGT + e$$

where:

P= Average three year post-privatization performance minus average three year pre-privatization performance (as measured by ROS, ROA, ROE, RS and NI). SLTA = Short-term Liabilities : Total Assets. LLTA= Long-term Liabilities : Total Assets. SOLD= Percentage of equity sold by government. EMPL = Share allocated on employee of the firm upon privatization. TOPMGT = A dummy variable that takes the value of 1 if there was change in Key top management like CEOs and the managing director and 0 otherwise.

Result And Analizyng

There are several factors identified in the literature that are possibly related to the performance changes between before and after privatization. Those factors consist of short-term and long-term debt assumed before the firm privatized, debt and percentage of equity sold at initial offer when the firms are privatized, changes in top management team in the company around the time of privatization, and shares allocated to employees at the offer. These factors are regressed on the several proxies of performance consisting of returns on sales (ROS), returns on assets (ROA), returns on equity (ROE), real sales (RS) and real net income (NI). The results of the test for the five regressions are presented in Table 1.

The significant independent variables vary across regressions for each model. When return on sales (ROS) is used as dependent variable, there are two independent variables that are significant namely, the short-run debts to total assets (SDTA) and the employee share ownership (EMPL).

The significant of SDTA as an independent variable to capture soft budget in general or subsidy in particular supports the proposition that, to some extent, soft budget constraint or subsidy which manifests in the form of short-run liabilities to assets ratio influences significantly the performance of firms upon privatization. This finding supports the theory of soft budget constraint introduced by Kornai (1980) who argued that soft budget constraints in the form of subsidies granted by governments as the main cause of the failure for many enterprises in the former Soviet Union and former communist countries of Central and Eastern Europe. Consequently, the budget should be hardened in order to discipline the managements of state-owned companies. However, the government should be cautious in implementing the policy as not too hard because as Frydman, Gray, Hessel and Rapaczynski (2000) noted, the supposedly "hard" budget constraints imposed by a government on state-owned enterprises are not very effective either.

Table 1

The Empirical Results of Regression Analysis on the sample of 30 privatized firms

	ROS[a]	t	ROA[a]	t	ROE[a]	t	RS[a]	t	NI[a]	t
Constant	-44.27	-2.26**	-19.45	-2.16**	-19.50	-1.29	0.57	0.16	7.75	3.47***
SDTA	21.30	1.76*	3.44	0.67	9.18	0.81	2.32	1.07	1.98	1.11
LDTA	9.91	0.95	1.59	0.35	-10.33	-0.91	0.34	0.20	2.34	1.46
SOLD	-0.59	-1.32	-0.27	2.01*	-0.42	-1.40	-0.07	-2.40**	0.02	0.04
LN_EMPL	3.33	1.77*	1.63	2.30**	1.55	1.32	0.78	3.64***	0.18	0.93
TOPMGT	-0.33	-0.06	-0.75	-0.37	7.72	2.49**	0.18	0.24	-0.57	-0.97
R^2	0.2590		0.2415		0.3025		0.3170		0.2360	
Adj R^2	0.1046		0.0834		0.1572		0.1747		0.0768	
F value	1.6778		1.5282		2.0820		2.2273		1.4823	
Prob F	0.1783		0.2185		0.1028		0.0845		0.2325	

Significant: *** at 1%, ** Significant at 5%, and * Significant at 10%.

The number of share allocated to employees has positive impact on the performance. Surprisingly, this result is contradicted with Frydman, Gray, Hessel, and Rapaczynski (1998) who uncover that different insider ownership has different performance; for employee-owned firms no discernable revenue effect could be found. Moreover, Lipton and Sachs (1990) argued that dominant ownership by employees could result in the perpetuation of existing inefficiencies. On the other hand, this finding is in line with Djankov and Pohl (1998) who find that privatization to insiders do not hamper firm restructuring. Further support comes from Smith, Cin and Vodopivec (1997) who find that employee ownership is associated with higher value-added.

This study proves that in Malaysia, the employee ownership has positive relationship with performance improvement which is inconsistent with evidences of Frydman et al. (1996) and Lipton and Sachs (1990). Owner employees in Malaysia are far from free rider owner instead they support the management toward achieving company's objectives by perhaps working harder or putting every effort toward company's success. It seems that the employees as the owners are aware they have to give support for their own benefits.

Long-term debts to total assets (LDTA), a proxy to capture soft budget constraints does not seems to effect performance change significantly. It is possibly that the soft budget is mainly accumulating in the form of short-term liabilities rather than long-term debts. The percentage of share sold (SOLD) by the government and the change in top management team (TOPMGT) is not significant either.

It is quite interesting that SOLD does not affect ROS. Public choice theory which predicts that the more control surrendered by a government leads to lesser government's interference on the management which in turn will improve efficiency. This insignificant finding presents ambiguous interpretation: there is a possibility that the government does not give up adequate control in privatization or, in other word, the government still intervenes with the management of the newly privatized companies so that the management does not have more freedom in managing the firm. It is also possible that the government indeed gave up some control but not as much as the percentage of ownership sold and hence, the higher percentage of share sold does not reflect the control hand over. This means that the assumption that the more the transfer of ownership the control is surrender is not fulfilled. Then, this finding may suggest that due to the government reluctance to not interfere with the management of the companies, partial privatization is not enough suggesting that complete or full privatization is warranted.

A number of studies report that the changes in top management affect the performance significantly (Barberis, Boycko, Shleifer and Tsukanova, 1996 and Dyck, 1997). The reasons for different finding of this study with those two earlier studies could be explained as follows. In Malaysian privatization, the change in top management does not occur right away when the privatization implemented. Instead the change in top management occurs around the time the privatization implemented; either one year prior or one year following the privatization. Moreover, less than half of the privatized companies change their top management position. This is a possible reason why this variable does not affect performance change upon privatization. It is worth considering that in privatization, the management should be replaced with the new team to get new management talent which at least will strive to perform better that old management. Furthermore, it is worth considering selecting professional management team even from outside the companies as many if not all the top management in old state-owned companies comes from governments sectors and many times they are government veterans.

The variable SOLD has negative effect on ROA which is inconsistent with the public choice theory. Public choice theory argues that the higher the equity ownership retained (lower percentage of equity sold) is the higher the possibility of the government's interference on the day to day firm's

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operation in the future which in turn will lead to a worse performance. Hence, the variable SOLD is predicted to have a positive impact performance. This finding is interesting and the following explanation could be possible. Malaysia government possibly chooses to interfere with day to day operation selectively despite the fact that the government owns the majority of share. It means that the managements of SOEs have, to some extend, an autonomy in managing SOEs. This fact is in contradiction with their counterparts in transition countries where the opposite findings were found. In the transition countries, directors of SOEs play a role very much similar as production line managers in the company without much control. As a result, the Malaysian SOEs that sell higher percentage of share do not necessarily produce a better performance. On the other hand, the SOEs in transition countries, once they are privatized, the managers get much control and freedom to manage the company and hence, more opportunity to improve the performance. Other explanation, Malaysia government may exercise certain degree of intervention but only for certain policy and in a positive manner. Therefore, the government interference in the SOEs in Malaysia does not lead to the worse performance of SOEs as reported in a number of literatures.

The positive effect of the variable EMPL is also inconsistent with the prediction. As predicted, based on enormous previous empirical studies, EMPL should have negative effect on performance. Again, the previous studies are mostly conducted in former transition countries of Eastern European nations. As already found in many studies, employee ownership was associated with worse performance. It has many things to do with the macro economic condition during the privatization era where the employees were not exposed to the free market such as in the western economy. As a result, the employees do not know what to do with their ownership other than taking advantage with assigning policies that were detriment to the companies such as raising wages etc. At the end, the employee ownership is not beneficial for the companies but instead worsening the performance of the company.

When ROE is used as dependent variable, only the change of top management in the companies has significant effect on ROE. This result is consistent with Barberis, Boycko, Shleifer and Tsukanova (1996) who argue that getting new managers (new human capital in their words) increases firm efficiency. Dyck (1997), in East Germany, shows that successful privatization hinges on the firm's ability to replace old and inefficient managers. It is argued that new manager will bring new expertise into the company or at least there is fresh new talent coming. Hence, the change in top management team or members of board of directors will lead to a better performance for the companies at least in the short-run because new comer almost always want to show his/her performance . When the dependent variable is substituted by real sale, the variable SOLD and Ln-EMPL are statistically significant. Of course, the significant effect of SOLD and Ln_EMPL on ROE has the similar explanation with the previous model.

Finally, when real net income is used as dependent variable, no one independent variable is significant. This result indicates that the data do not support the model and hence, combinations of all independent variables are not able to explain the variation in real net income. In short, out of five independent variables, only long-term debt to total assets has never been statistically significant for all different models. It indicates that long-term debt to total assets does not have any effects on the performance of firms upon privatization.

The variations on the post-privatization performance of state-owned enterprises could be explained by several factors. When the Return on sales used as the dependent variable, the explanatory variables are Short term Debt to Total Asset and Ln Employee; when Return on Asset used as the dependent variable, fraction of ownership sold and Ln Employee; when Return on Equity used as dependent variable, top management change, real sales, fraction sold and Ln employee; and when Net Income used as dependent variable, none is significant.

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