THE EFFECT OF PRIVATIZATION ON FIRM FINANCIAL PERFORMANCE IN KENYA

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DECLARATION

This research project is my original work and has never been submitted for a degree in any University.

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This project has been forwarded for the purpose of examination with my approval as the university supervisor.

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Dr. Sifunjo Kisaka

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DEDICATION

My heart felt dedication goes to my dear parents who have been a great source of inspiration since my childhood.

ABSTRACT

This study aimed at establishing the effect of privatization on firm financial performance in Kenya. The study was based on the financial reports of six firms which were privatized within the period 1991 and 2008. The analyses covered a period of three years before and after privatization for each of the firm, and the mean and standard deviation on returns on turnover, total assets and equity were the key statistics performed on the data from those firms. The study found out that the firms improved their performance after privatization. The Government should therefore move away from pursing commercial activities and instead concentrate in activities such as provision of services and creating the legal and institutional framework conducive to increased private investment.

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LIST OF ABBREVIATIONS

CEO	Chief Executive Officer
HFCK	Housing Finance Company of Kenya Limited
KENGEN	Kenya Electricity Generating Company of Kenya Limited
KEN RE	Kenya Reinsurance Corporation Limited
KQ	Kenya Airways Limited
MSCL	Mumias Sugar Company Limited
NBK	National Bank of Kenya Limited
ROE	Return on Equity
ROT	Return on Turnover
ROTA	Return on Total Assets
SOEs	State Owned Enterprises
STDEV	Standard Deviation

CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Privatization is the deliberate sale by a government of state-owned enterprises (SOEs) or assets to private economic agents. Megginson and Netter (2001) noted that privatization had been in use worldwide since its introduction by Britain's Thatcher government in the early 1980s to a then-skeptical public and has been accepted as a legitimate tool of statecraft by governments of more than 100 countries. They observed that privatization had become an important element of the continuing global phenomenon of the increasing use of markets to allocate resources and was tempting to point to the spread of privatization programmes around the world during the past two decades and conclude that the debate on the economic and political merits of government versus private ownership had been decided. However, they steered clear of making such a conclusion as it would have been flawed since twenty-five years ago proponents of state ownership could just as easily surveyed the postwar rise of state-owned enterprises and concluded that their model of economic organization was winning the intellectual battle with free market capitalism.

Throughout history, there had been a mixture of public and private ownership of the means of production and commerce, observed Sobel (1999). State ownership of the means of production, including mills and metal working, was common in the ancient Near East, while private ownership was more common in trading and money lending. In ancient Greece, the government owned the land, forests, and mines, but contracted out the work to individuals and firms. In the Ch'in dynasty of China, the government had monopolies on salt and iron. In the Roman Republic the private individuals and companies fulfilled virtually all the of the state's economic requirements. Rondinelli and Iacono (1996) noted that by the time of the Industrial Revolution in the western industrialized societies and their colonies, the private sector was the most important producer of commercial goods and was also important in providing public goods and services. This pattern, with more government involvement in some countries and less in others, continued into the twentieth century in both Western Europe and its colonies and former colonies. In the United States, there was less government involvement than many other countries.

According to Porta et al (2002) the Depression, World War II, and the final breakup of colonial empires pushed government into a more active role, including ownership of production and provision of all types of goods and services, in much of the world. In Western Europe, governments debated how deeply involved the national government should be in regulating the national economy and which industrial sectors should be reserved exclusively for state ownership. They observed that until the Thatcher government came to power in 1979, the answer to this debate in the U.K and elsewhere was that the government should at least own the telecommunications and postal services, electric and gas utilities, and most forms of non-road transportation, especially airlines and railroads. Many politicians also believed the state should control certain "strategic" manufacturing industries, such as steel and defense production. In many countries, state-owned banks were also given either monopoly or protected positions.

However, Rondinelli and Iacono (1996) observed that in the developing world, government ownership was perceived as necessary to promote growth. In the postcolonial countries of Asia, Africa, and Latin America, governments sought rapid growth through heavy investment in physical facilities. Another reason for government ownership, often through nationalization, was a historical resentment of the foreigners who had owned many of the largest firms in these countries.

1.2 Privatization in Kenya

From 1963 when Kenya achieved political independence, the Government's participation in commercial activities grew rapidly and broadly resulting in state dominance in various forms (including monopolies) in many commercial activities. The establishment of the parastatals was driven by a national desire to: accelerate economic social development; redress regional economic imbalances; increase Kenyan Citizen's participation in the economy; promote indigenous entrepreneurship; and promote foreign investments (through joint ventures). This desire was expressed in the Sessional Paper No. 10 of 1965 on African Socialism and its application to planning in Kenya.

The Sessional Paper guided nationalization under which a few private sector operations were brought under government control. It pointed out that nationalization was only needed when the assets in private hands threaten the security or undermine the integrity of the nation; or when productive resources are being wasted; or when the operation of an industry by private concerns has a serious detrimental effect on the public interest; or when other less costly means of control are not available. The paper indicated that once in government hands the nationalized operations had to operate efficiently, cover costs and earn profits at least equivalent to taxes paid when operating efficiently. It also emphasized the complementary role played by private sector in creating additional productive assets for the country and employment and the need to utilize government resources in areas in which private sector is unable and unwilling to invest.

The Report on Review of Statutory Boards (1979) pointed out that: the growth in the parastatal sector had not been accompanied by development of efficient systems to ensure that the sector plays its role in an efficient manner; there was clear evidence of prolonged *inefficiency, financial mismanagement, waste and malpractices in many parastatals;* government investments had largely been at the initiative of private promoters with government being brought in either as an indispensable partner or to undertake rescue measures; many of the parastatals had moved away from their primary functions, especially the regulatory boards most of which had translated their regulatory role into executive one, resulting in waste and confusion; and there was danger of over-politicizing production and distribution through establishment of too many parastatals.

The Report on the Working Party on Government Expenditures (1982) pointed out that: Kenyanization had remained merely presentational through government ownership; state corporations' operations had become inefficient and unprofitable, partly due to multiplicity of objectives; existence of parastatals in commercial activities had stifled private sector initiatives; and many of the joint ventures had failed, requiring the government to shoulder major financial burden. The Report on the Working Party on

Government Expenditures concluded that some of the resources diverted to the government to finance the state corporations' activities could have contributed more to national development if these state corporations were left in the private sector. The report recommended that: the government should act as a creator of favourable setting within which people can develop themselves and the economy; the government should divest from its investments in commercial and industrial enterprises to transfer active participation to more Kenyans through participation in shareholding; the government should reduce exposure to risk in areas in which the private sector can assume risk without government intervention; the government should dismantle some of the existing administrative hurdles which discourage private sector initiative and provide needless opportunities for corruption; and the government should reorganize legal and institutional framework regarding monitoring and supervision of parastatals.

The Sessional Paper No.4 of 1991 on Development and Employment in Kenya decried the continued deterioration of the performance of state corporations. The Paper pointed out that while the creation of state corporations through which government participation in economic activities was appropriate soon after independence, the objectives for and the circumstances under which most of the state enterprises were created had since changed. The paper underlined the need to implement privatization and divestiture of state corporations urgently in view of the managerial problems afflicting the parastatals leading to poor return on government investments. It pointed out the existence of a larger pool of qualified manpower, the availability of more indigenous entrepreneurship to permit private sector led economy and the need for non-tax revenue for the Government.

The Policy Paper on Public Enterprises Reform and Privatization (1994) outlined the institutional framework and the guidelines and procedures to be applied in privatizing state corporations. The paper pointed out that there were 240 commercial public enterprises with public sector equity participation and classified the public enterprises into two categories: 207 non strategic commercial public enterprises which were to be privatized and 33 strategic commercial public enterprises which were to be restructured and retained under public sector ownership and control.

The 1998 version of the Policy Paper on Public Enterprises Reform and Privatization shows that by 30th September 1998 of the 207 non strategic commercial public enterprises 145 had been privatized as follows: 12 were liquidated; 14 were sold through receiverships; 53 through pre-emptive rights; 8 through public flotations; 14 through competitive bidding; 1 through management buyout; 5 through partial divestitures; and 39 through complete divestitures. The Privatization Programme (2008) notes that most of the non strategic commercial enterprises had been privatized either fully or partially by the end of the first phase of the programme in 2002.

Cook and Kirkpatrick (1995) stated that privatization is one of the several policy options for promoting improvements in SOEs performance and can take a variety of forms each with a different impact on the objectives of privatization policy. They stated that SOEs can be privatized in a number of ways. The different methods of privatization can be grouped into two categories: methods involving the sale of enterprise (divestiture) - public flotation, private sale and management buyout; and methods involving transfer of control from public to private sector - contracting out, management contract and leasing and franchising. Each of these privatization methods contributes in varying degrees to the government's privatization objectives. The choice of the method used will vary with the objectives and constraints prevailing in each case.

1.3 Problem Statement

Cook and Kirkpatrick (1995) observed that despite the difficulty of measuring public enterprise performance, one of the main reasons for the drive towards privatization had been the poor financial performance of SOEs. Privatization was being driven by a pragmatic reaction to over three decades of poor financial performance by SOEs. Private ownership was thus favoured, on the grounds that returns to capital were lower among SOEs and they generally had a poor reputation for innovation, diversification and quality of goods and services.

According to Nellis (2006) many public enterprises performed poorly. Rather than contribute to state budgets, they drained them. A high percentage failed to produce a sufficient quality or a high quality of service or a product. He noted that there was widespread failure to charge cost covering tariffs in infrastructure/utility public enterprises; and subsidies from government and soft budget kept the enterprises afloat. These flows eventually posed large financial burdens on government budgets and thus attracted the attention of the international financial institutions and donors.

Nellis, further observed that most governments were finding it more difficult to provide their infrastructure firms with capital needed for maintenance and expansion. Much of the improvement resulting from privatization came from the ability of the new private owners to tap private capital markets. Strained public funding was not sufficient to meet repair and expansion needs. Private operators were more able to raise investment capital from private markets.

Aseto and Okelo (1997) noted that privatization in Kenya was being undertaken because there was general dissatisfaction with the performance of many state-owned enterprises: the enterprises had failed to meet popular expectations for product quality or quantity; many of them had been too ambitious in their product lines or unable to deliver on time; a large number of the enterprises had been unable to compete with the already flourishing private sector; and the technological advances had made some of the products or services provided by the enterprises obsolete. Moreover, the changing world markets or differing consumer tastes had made products of these enterprises more difficult to market. They therefore concluded that the government felt privatization could be justified as a way of meeting the changing consumer demand.

Poorly performing public enterprises, sheltered from market competition and enjoying preferential access to scarce inputs, have limited the growth of the enterprises, increasing their costs of business and blocking their access to markets. The Government has had to shoulder heavy fiscal and managerial burdens, absorbing an increasing share of the scarce public resources. This has consequently called for measures which would ensure the public enterprises become more responsive to market forces and the price mechanism. The reform efforts that have been instituted to make the public enterprise sector more responsive to market forces and price mechanism are threefold: market liberalization;

enterprise reform (restructuring); and privatization. In Kenya key in the reform efforts has been privatization. The various studies that have been carried out on privatization and related fields in Kenya include: Nyong'o et al (2000) The Context of Privatization in Kenya; Debrah and Toroitich (2005) The Privatization of Kenya Airways, a case study ; and Odipo (2010) Whether Privatization has Achieved its Objectives in Kenya, a case of firms privatized at Nairobi Stock Exchange. No study has been carried out on the effect of privatization on firm performance in Kenya. This study aims at establishing the effect of privatization on firm financial performance in Kenya. Therefore, the question that remains unanswered is whether privatization has resulted in improvement in the financial performance of the privatized enterprises. This study will analyze the financial performance of the privatized firms in Kenya before and after privatization. The results of the study will give an indication as to whether privatization should be encouraged as a reform strategy or discouraged.

1.4 Objective of the Study

This study aims at determining the effect of privatization on the firm financial performance in Kenya.

1.5 Significance of the Study

The study will benefit the Government in that if the firms' performance is revealed to have improved, then the Government will not be required to finance the firms' activities through the tax revenue. The Government can then use the revenue so saved to provide services to the citizens.

The other beneficiaries of this study are the investors who acquired shares in the privatized firms. The performance of the firm as revealed by the study will give an indication of whether their investment in the firm is a gain or loss. The dividends distributed by the firms represent a direct return on the investment by the shareholders. Improved financial performance by the privatized firms will mean higher dividend to the shareholders and thus more income at their disposal. The improved financial performance will lead to higher price for the firms' shares. Improved share price represents a capital gain to those who may choose to dispose of their investment in the firms.

The tax authority would benefit from this study in that it would show the performance of the privatized firms. Where the privatization results in improved performance of the firms, this will mean more revenue to the tax authority in that more profits of the firms will be subjected to tax. Further, the distribution of dividends to the individual investors would represent additional revenue in that the recipients would attract additional tax.

Sale of enterprises through stock exchanges broadens the base of share capital hence stock market will develop, because general public will be in position to purchase the shares of the privatized firms and investment opportunities for general public will increase.

There are always political pressures on Government owned industries, banks and other institutions for employment of political workers and loan facilities from banks. When these enterprises have gone into the hands of private owners then these pressures will be reduced to a great extent.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Literature review is an evaluation of the information found in the literature related to the selected area of study. This Chapter reviews the various studies conducted on privatization. Section 2.2 reviews the theories on privatization; section 2.3 reviews the performance of public enterprises in Africa; section 2.4 reviews the mechanisms for improving public enterprise performance and section 2.5 reviews the empirical evidence on privatization and public enterprise performance. Section 2.6 gives a summary of privatization in the developing countries.

2.2 Theories on Privatization

The normative theories justifying privatization as a direction for public policy draw their inspiration from several different visions of a good society, noted Starr (1989). The most influential is the vision grounded in laissez-faire individualism and free-market economics that promises greater efficiency, a smaller government, and more individual choice as the domain of property rights and market forces is expanded. The second vision is rooted in a more socially minded conservative tradition, that promises a return of power to communities through a greater reliance in social provision on families, churches, and other largely nonprofit institutions. Privatization, in this view, means devolution of power from the state to ostensibly non-political and non-commercial forms of human association. The third perspective sees privatization as a political strategy for diverting demands away from the state and thereby reducing government "overload."

The property rights theory as developed by Demsetz (1967), Alchian (1977), Eggertsson (1990) and Barzel (1997) explains differences in organizational behaviour solely on the basis of the individual incentives created by the structure of property rights. In this view, property rights specify the social and economic relations that people must observe with each other in their use of scarce resources, including not only the benefits that owners are allowed to enjoy but also the harms to others that they are allowed to cause. A right of ownership actually comprises several rights, chiefly the rights to use an asset, to change it in form, substance, or location, and to transfer all or some of these rights. Insofar as the state restricts these rights, they become "attenuated." Thus the key issues for the theory are: to whom are property rights assigned? and how, if at all, are they attenuated?

The property rights school conceives of human action as purely individualistic. The more individuals stand to gain from tending to their property, the better will it be tended. Conversely, the more attenuated and diluted their property rights, the less motivated individuals will be to use property under their control efficiently. Private ownership concentrates rights and rewards; public ownership dilutes them. The property rights school does not recognize any fundamental change in the working of private enterprise as a result of the separation of ownership and management in the modern corporation. To be sure, shareholders in large corporations cannot monitor management as closely as the owner of the classical firm could oversee his enterprise. However, in this view, the market generates the needed spur to prevent corporate management from dissipating value through excessive salaries or slack attention. If returns from the enterprise are low, shareholders will sell their stock and the price will be depressed. In the extreme case, the firm may be acquired by outsiders and the managers may lose their jobs. These crucial deterrents to inefficient management are missing from the public sector. Since "shareholders" (citizens) have no transferable property rights in public enterprise, they cannot sell stock as a signal of dissatisfaction with performance; even moving to another jurisdiction is costly. Moreover, there is no "market for corporate control"; public enterprises cannot be taken over by bidders who believe that they can make more efficient use of the assets. Hence, according to the theory, there is no check on the dissipation of value by the management of public enterprises.

Public choice theory, as developed by Downs (1957), Black (1958), Buchanan and Tullock (1962) Arrow (1963) and Niskanen (1971), focuses on political considerations of both the public and private enterprises subject to political influence. It involves a political game between the public, the politicians, and the enterprise managers. Each category of actors has their expected utility functions, and seeks to maximize these utilities but none have access to identical information. With the asymmetry of information, the politicians may find that improving the economic efficiency of the firm may not improve their electoral prospects; rather they find it to their advantage to set the prices at below marginal cost so that their chances of electoral success are enhanced. In the utility function of the bureaucrats the size of the departmental budget and the rents that accrue to them occupy a predominant role. Since payoffs are an increasing function of the budget size, the bureaucrats' interest would lie in procuring as large a budget as possible. They may be aided in their endeavor by the politicians, since the welfare of ministers can be expected to be positively linked to that of the bureaucrats. The consequence is internal inefficiency. The public managers themselves can secure higher pay, greater power and prestige than their private sector counterparts by forming coalitions with politicians and bureaucrats. As a result, social objectives get to be replaced by political objectives, political interventions are made in managerial decisions, and imperfections ensue in the incentive structure of publicly-owned firms.

The community empowerment theory of privatization emphasizes the strengthening of communities. In the most noteworthy exposition of this position, Berger and Neuhaus (1977) propose that government "empower" voluntary associations, community organizations, churches, self-help groups, and other less formal "mediating" institutions that lie between individuals and society's "alienating mega-structures." In their view, the modern liberal state has undermined these "value-generating," "value-maintaining," "people-sized institutions" by establishing service bureaucracies that take over their functions. Berger and Neuhaus are not opposed to the provision of social welfare, but they urge that, wherever possible, public policy rely on mediating institutions for the delivery of publicly financed services. Their concern is not to expand the domain of the profit motive but rather to strengthen local, small-scale forms of social provision. This is privatization with a human face, and it bears some resemblance to interest in community organizations and cooperatives.

The reduction of government overload theory of privatization holds that privatization is desirable for its likely political effect in deflecting and reducing demands on the state. In the 1970s, some critics, most notably, Rose (1984) suggested that the Western democracies were suffering from an "overload" of pressure, responsible for excessive spending and poor economic performance. In that framework privatization represents one of several policies encouraging a counter-revolution of declining expectations. In a similar vein, Butler (1985) argued that privatization can cure budget deficits by breaking up the kind of public spending coalitions described by public choice theory. Privatizing government enterprises and public services, in this view, will redirect aspirations into the market and encourage a more entrepreneurial consciousness.

2.3 Performance of Public Enterprises in Africa

State-owned enterprises (SOEs) comprise a large and rapidly growing sector of the economy in the majority of countries in the world, observed Aharoni, (1982). He further noted that they had been created for a variety of reasons which included: spearheading industrialization in countries with virtually no large-scale industry; promotion of industries deemed to be of strategic importance; creating lines of activities with no sufficient incentive for private investment; establishing projects which require huge amounts of capital, not easy to raise privately within the present structure of the capital markets; saving of threatened jobs; reducing the presence or preventing the entry of foreign-owned firms; expanding the public sector; raising more revenue for the government to finance development, capital expenditure, or current expenditure; avoiding the evils of private monopoly over strategic industries; securing the sale of goods and services at reasonably low prices, particularly for the poorer customers; and other social or political reasons.

The performance of the state-owned enterprises had, in general, been poor, observed Ray (1980). In particular: financial rates of return had generally been lower for public enterprises than for the private sector; financial profitability had been compromised by price controls; public enterprises had often put large burdens on public budgets; state-owned enterprises contributed to the augmentation of the external debt of many developing countries; and countries in which public enterprises accounted for higher shares of gross domestic investment generally had lower rates of economic growth.

According to Ayub and Hegsted (1987) a number of reasons accounted for the poor performance of public enterprises, among them lack of incentives on the part of management. Few countries had used performance bonuses or profit sharing to motivate top management. Also, in some countries, managers were part of the civil service or at least subject to its pay scale. Even where this was not the case, their pay seldom matched private salaries. Although the prestige and challenge of running what were often the largest corporations in the country would sometimes compensate for lower pay, low salaries tended to deter skilled managers and increase staff turnover, noted Ayub and Hegsted.

Shortage of competent managers was another reason for the poor performance, observed Nellis (1986). He noted that the growing number of public enterprises in many Sub-Saharan African and other countries, had contributed to a chronic shortage of management. This shortage had been sometimes exacerbated by programme for rapid indigenization. Many senior posts were left vacant or were filled by unqualified staff. The organization thus became too dependent on its chief executive. The shortage of managers also contributed to a high rate of turnover as competent people were shifted around to head troubled government enterprises. Even countries without a managerial shortage changed the managers of the state-owned enterprises with damaging frequency if selection of top managers was based on nepotism or political patronage, Nellis further noted.

Another reason for poor performance was lack of competition. According to Mahmoud (1992) many state-owned firms were monopolies producing goods and services that were not traded internationally or that the government preferred to produce domestically for reasons of national security or public interest. In other cases the economy was too small to support another domestic producer. Also, managers were not given discretion to respond to competitive pressures which would mean reducing staff or ending unprofitable service.

A further contribution to poor performance, Mahmoud noted, was the little emphasis on profitability and efficiency by governments. The public enterprises were not instructed to maximize profits or even to minimize costs since adjusting administered prices typically involved practical and political problems. Further, state-owned enterprises were often required to perform noncommercial roles such as hiring extra staff to increase employment or setting up a plant in a particular area to promote regional development or entering into a completely different line of activity to achieve diversification. These conflicting goals often reduced profits.

According to Vernon and Ahoroni (1981) only a few countries applied organized public pressure as a way of increasing the efficiency of public enterprises. Also, governments seldom took action to remove inefficient managers of these enterprises. Moreover, governments were rarely prepared to use the sanction of liquidation. This lack of effective accountability contributed to poor performance by the public enterprises.

All too often, different government agencies intervened in state-owned enterprises decisions that should be the prerogative of management, observed World Bank (1991), and yet management fails to coordinate their action. In addition, policy that swings between autonomy and central control could prevent coherent direction of public enterprises. Many attempts to reduce arbitrary intervention by government had become counterproductive, substituting one form of bureaucratic intervention for another.

In many developing countries the internal management information systems of public enterprises were deficient or non-existent, noted World Bank (1991). The companies were not audited according to uniform standards. This was due to lack of a trained body practitioners and qualified accountants as well as lack of active plans designed to focus efforts on improving efficiency and monitoring results. Public enterprises were frequently expected to contribute to the broader goals of government policy. The consequences could be perverse. For instance, public enterprises' prices could be controlled to benefit the poor or to assist counter-inflationary policies. But these firms' consumers were often large industrial users or wealthy people, so they did not benefit the poor most. It is estimated that three-quarters of the energy and food subsidies in Egypt went to the relatively more affluent urban areas and about two-thirds of these went to the richer half of the urban population, observed World Bank.

According to Kay et al (1986) the main objectives of privatization could be summarized thus: the reduction of the state sector; promotion of wide share ownership; greater efficiency within privatized entities, coupled with profit motivated decisions; raising revenue for the government; reduced government interference, increasing speed of decision making; introduction or enhancement of competition; exposure to the disciplines and opportunities of private sector markets for capital and other resources. These objectives needed not be equally important for all state-owned enterprises. Also, these goals were not mutually exclusive. Obviously, the government in each country needed to consider local factors and individual industry circumstances in determining the mix of goals, noted Kay et al.

2.4 Mechanisms for Improving Public Enterprise Performance

In many developing countries there was widespread concern with the poor public enterprise performance, and it was generally agreed that reform of the sector was needed urgently, observed Cook and Kirkpatrick (1995). They noted that reform efforts were centered on measures which were intended to make the public enterprise sector more responsive to market forces and the price mechanism. Thus they put forward three main policy strategies for improving the economic performance and contribution of the public enterprise sector: market liberalization; enterprise reform (restructuring); and privatization.

According to Cook and Kirkpatrick (1995) market liberalization refers to changes in the policy framework within which the public enterprises operate, which will create a more competitive, market oriented environment. The liberalization can cover macroeconomic policies, the labour market, and the legal and regulatory framework. Enterprise reform refers to internal changes in the management, organization and operational practices of public enterprises. These can include improving fiscal discipline and control and management by for example improvements in financial monitoring and reporting, greater managerial accountability, increased enterprise autonomy in pricing and purchasing, and clarification of enterprise objectives. Privatization refers to the transfer of ownership and/or control of productive assets from public to private sector. Privatization can take a number of different forms, and can be partial or outright. The most common form of privatization involves ownership transfer, but it is also possible to have privatization of control, with ownership remaining in the public sector.

2.5 Empirical Evidence on Privatization and Public Enterprise Performance

Few studies have examined the operating and financial performance of newly privatized firms in developing countries. The existing empirical literature has focused on the experience of developed countries with the notable exceptions of Galal et al (1994), Megginson et al (1994), Boubakri and Cosset (1998) and D'Souza and Megginson (1999). In a World Bank study, Galal et al (1994) assess the welfare gains or losses resulting from the privatization of 12 companies operating mostly in non-competitive markets in 4 countries: Chile, Malaysia, Mexico and United Kingdom. They reported net welfare gains in 11 of the 12 cases. Productivity increased in 9 of the 12 cases and remained unchanged in the other 3. The methodology involved allocation of the costs and benefits of adjustment among different economic groups. The analysis revealed no case in which workers lost overall from privatization. They claimed that the results provided evidence in support of net welfare gains even when they tried to isolate the effect of privatization from the effects of other factors such as changes in market structures and in macroeconomic conditions. However, their sample was small and unrepresentative of the universe of privatized firms in developing countries and any generalization of their evidence should be avoided.

In contrast, a major study by Megginson et al (1994) compared the pre- and post-privatization financial and operating performance of 61 firms from 18 countries (12 industrialized and 6 developing (non-industrialized) and 32 industries over the period, 1961-1990. The methodology involved comparing real sales, investment spending and operating efficiency. They presented strong evidence that, following privatization, their sample firms became more profitable, increased their real sales and their investment spending and improved their operating efficiency. The companies significantly lowered their debt levels and increased dividend payments. More surprisingly, they found no evidence that employment levels declined after privatization. Instead, they reported an increase in the mean and median employment and they found that 64 percent of the sample companies employed more workers after privatization. Their results were generally unchanged when they partitioned the data into smaller sub-samples and compared the financial and operating performances of fully versus partially privatized firms, privatized firms operating in competitive versus noncompetitive industries, and (industrialized) versus non-industrialized (developing) country firms. They documented important changes in the size and composition of the board of directors for the newly privatized firms in their sample. However, the sample included only a small number of firms headquartered in developing countries. Depending on the financial and operating performance measure, the number of sample firms operating in developing countries ranged from 3 to 12. Therefore, the sample size was too small to consider that the reported evidence reflected the actual experience of privatizations in developing countries.

Boubakri and Cosset (1998) considered a large set of newly privatized firms (79) headquartered in 21 developing countries that experienced full or partial privatization over the period 1980 to 1992. Their sample covered a wide range of developing countries in terms of development level and capital market sizes. Their sample included countries identified as low-income economies (Bangladesh, India, Pakistan), lower-middle-income economies (Chile, Jamaica, Nigeria, Philippines, Thailand, Tunisia, Turkey) and upper-middle-income economies (Argentina, Brazil, Greece, Malaysia, Mexico, Portugal, Singapore, South Korea, Taiwan, Trinidad and Tobago, Venezuela). The sample also included firms operating in competitive and non-competitive markets. In addition to companies privatized through public share issues considered by Megginson at el, their sample also included companies privatized through direct sale to another company, a frequently-used method in developing countries. In their methodology they compared operating efficiency, capital investment, real sales, total employment and dividends. In addition they used both raw and market-adjusted performance measures so as to isolate the effect of privatization from the impact of macroeconomic changes on the financial and operating performance of SOEs. For both unadjusted and market-adjusted performance measures they found that newly privatized firms exhibited significant increases in profitability, operating efficiency, capital investment spending, real sales, total employment and dividends. They also documented a decline in leverage following privatization but this change was significant only for unadjusted leverage ratios. Additionally, their results were generally robust when they partitioned their data into various sub-samples such as full versus partial privatizations, control versus revenue privatizations, companies operating in competitive versus non-competitive industries and companies based in upper-middle-income countries versus low-income and lower-middle-income countries. However, their evidence suggested that privatization yielded greater benefits for companies operating in developing countries with high income per capita and for companies whose governments surrendered voting control.

D'Souza and Megginson (1999) compared the pre- and post-privatization financial and operating performance of 85 companies in 28 countries and 21 industries that were privatized through public share offerings for the period from 1990 through 1996. Out of these 85 companies, 58 of the firms were from 15 industrialized countries and 27 from 13 developing countries. The methodology involved comparing output, operating efficiency, and dividend payments. They documented significant increases in profitability, output, operating efficiency and dividend payments and significant decreases in leverage ratios for their full sample of firms after privatization. These results were generally unchanged when the full sample was partitioned into the following sub-samples: firms headquartered in an industrialized or developing country, firms whose voting control was sold or retained by the divesting government, firms operating in a competitive or non-competitive industry, firms with or without a large scale (at least 50 percent) turnover in the firm's board of directors after privatization, firms whose CEO was retained or replaced after privatization. In contrast to Megginson et al (1994) they found insignificant changes in the capital expenditures to sales measures in the post privatization period (as Boubakri and Cosset, 1998). They concluded that their results combined with those of Megginson et al (1994) and Boubakri and Cosset (1998) suggested: that privatization improved the financial and operating performance of newly divested firms; that these improvements were the results of socially beneficial improvements in productive efficiency and entrepreneurial effort; and that privatization worked in a wide variety of countries, industries and competitive environments.

2.6 Summary

State-owned enterprises exist in all countries: developing and developed; market and socialist, observed Mahmoud (1992). They produce a broad range of goods and services such as power, communications, steel, fertilizers, automobiles and petrochemicals. He noted that their performance varies widely within and between countries, but their record had frequently been poor, particularly in developing countries. They have clearly failed to play the strategic role in industrialization that governments had hoped for. He further noted that governments in industrial and developing countries alike were divesting their ownership of public enterprises through liquidation which involves the closure of the enterprise, or the suspension of some or all of its operations, privatization of management using leases and management contracts, or privatization of ownership through the sale of assets to the private sector to improve efficiency and competition.

The essence of privatization in Africa was the acknowledgement by governments that it was not their business or responsibility to run enterprises. State-controlled businesses tended to be insufficient entities run with insufficient commercial acumen. Historically, to offset losses, governments in Africa subsidized these enterprises with taxpayer's money which should be spent on improving social services delivery. Many African countries now recognize that they need privatization to help them to develop capital markets, observed Kabote (2011).

Privatization on the African continent had been progressing more slowly mainly because African countries were severely inhibited by environmental weaknesses in their efforts to privatize, namely embryonic capital markets, scarce financial resources, a weak private sector, and poor prudential regulation, observed Tanyi (1997). The relatively low per capita income and risk aversion, acute asymmetries of information, poor investment incentive structures and general institutional instability were some of the most serious obstacles to the development of securities market in Africa, and the pursuing of privatization. Therefore, implementing privatization in Africa presented serious sociopolitical challenges because it was widely perceived on the continent as a euphemism for unemployment, reduced government spending on social programmes and to the extent that foreign investors participate and make windfall profits, noted Tanyi.

As far as the methods of privatizations were concerned, they were largely determined by the objectives of the government and the particular need of the country, observed Sader (1994). Hence, the large variety of the ways privatization was implemented. Some countries, resorted to public offerings that is, the sale of shares to the general public to spread ownership, while others sold shares or assets of SOEs mainly to private investors (permitting certain ownership structures). According to Berg and Shirley (1987) the level of development of the capital markets in a country also determines whether certain privatization methods can be applied. For example, if the local stock market is thin, the public offering of shares is often not feasible. In this case, private sales of SOEs to local and foreign investors are likely to become the predominant method of divestiture.

In Africa, the foreign investor participation is a sensitive issue associated with the perception of re-colonization, Dinavo (1995) observed. Further, the effect that privatization could possibly have on the already skewed wealth dynamics explained to a large extent why governments had been slow in implementing privatization policies. Indeed, privatization could worsen the already existing socioeconomic inequalities across the population and could exacerbate the patronage largely based on ethnicity. In this context, one main factor inhibiting privatization relates to the identity of potential buyers in newly privatized firms, such as the ruling elite or certain ethnic groups. For example, Indians in East Africa make up disproportionate numbers of potential domestic buyers of public assets while other privileged groups composed especially of resident foreigners and politically disadvantaged but economically strong ethnic regional or religious groups dominate in much of West Africa.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlines the general methodology that the researcher used to conduct the study. Section 3.2 gives the research design; section 3.3 describes the population; section 3.4 describes the sample and the sampling procedure; section 3.5 gives the data collection method and section 3.6 outlines the data analysis procedure.

3.2 Research Design

The researcher adopted a quasi-experimental (event-study) design to carry out the study. The researcher observed the pre-privatization performance and the post-privatization performance of the various SOEs in Kenya that have been privatized during the period 1991 and 2008.

3.3 Population

Mugenda and Mugenda (1999) define a population as a complete census of all items or people in a researcher's area of study. The population of the study was the companies which were previously either wholly or substantially owned by the Kenya Government, but in which now the Government's ownership has been diluted within the period 1991 and 2008. The population for the study consisted of 152 companies.

3.4 Sample and Sampling Procedure

The study was based on the financial reports of the selected firms in which the Kenya Government has disposed of its equity holding during the period 1991 and 2008. To draw the sample size the firm must have been in operation for at least three years before the privatization and continued in operation for three years after the privatization. Most of the firms were privatized through liquidations and receiverships as most of them were already experiencing financial problems. Using this criterion a sample of six firms were selected for review.

3.5 Data Collection

Secondary data consisting of annual financial reports were collected from either the individual firms selected or the Investment Department of Treasury. Data forms were designed to record the key data items for the period of six years reviewed by the study for each of the selected firms. The data listed in these forms provided the necessary items used in the computation of the various ratios such as return on turnover, return on total assets and return on equity. These ratios were key indicators of a firm's financial performance. The aim was to come up with valid empirical evidence on comparison of financial performance before and after privatization of the selected firms.

3.6 Data Analysis

To compare the performance of the selected firms before and after privatization, descriptive statisics such as mean and standard deviation was used. Microsoft Excel Software was used to carry out the data analysis.

3.6.1 Analytical Model

An event study, in finance research, is an analysis of whether there was a statistically significant reaction in financial markets to past occurrences of a given type of event that is hypothesized to affect public firms' market values. The event that affects a firm's market value may be within the firm's control, such as the event of the announcement of a stock split. Or the event may be outside the firm's control, such as the event of a legislative act being passed, or a regulatory ruling being announced, that will affect the firm's future operations in some way.

In the study the event was privatization. Financial data of six companies in which the Government disposed of its equity holding within the period, 1991 to 2008, was analyzed. The analyses covered a period of three years before privatization and three years after privatization for each of the chosen corporations.

3.6.2 Diagnostic Tests

Descriptive statistics such as mean and standard deviation was used to test the data for its ability to be relied upon for valid conclusion. These tests were applied on all the data for the pre-privatization and post-privatization periods.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the results of data analysis and their discussion. Section 4.2 gives the summary statistics by use of the mean and the standard deviation; section 4.3 presents financial performance of the privatized firms using financial ratios such as return on turnover, return on total assets and return on equity; section 4.4 gives a discussion of the results using summary statistics and financial ratios and section 4.5 presents the summary of the findings.

4.2 Summary Statistics

All the firms reviewed by the study are analyzed as a single unit to see the effects of privatization for the period before and after privatization. The mean and standard deviation on the three measures of performance used are calculated for the period before and after privatization and are shown in Table 4.1.

Table 4.1 Firm's Performance on the Basis of the Mean and Standard Deviation of the Return on Turnover, Return on Total Assets and Return on Equity

Before Privatization					After Privatization		
		Ratio			Ratio		
Firm	Year	ROT	ROTA	ROE	ROT	ROTA	ROE
	1	33	5	61	17	2	44
	2	18	2	29	30	4	88
KENGEN	3	16	2	32	15	2	38
	1	16	0	56	17	3	63
	2	30	1	25	16	3	48
HFCK	3	16	1	14	17	3	52
	1	-2	-2	-14	8	1	6
	2	0	0	-3	-3	-2	-21
MSCL	3	6	8	62	8	9	78
	1	8	1	94	28	2	37
	2	4	1	88	9	2	50
NBK	3	3	1	14	6	1	39
	1	-9	-14	-73	8	8	37
	2	0	-1	-2	11	10	57
KQ	3	17	33	67	9	7	52
	1	21	5	33	28	11	99
	2	26	7	50	25	9	89
KEN RE	3	11	3	26	23	9	103
MEAN		**11.89**	**2.94**	**31.06**	**15.11**	**4.67**	**53.28**
STDEV		**11.57**	**8.81**	**39.92**	**9.01**	**3.83**	**31.26**

Note: ROT is Return on Turnover; ROTA is Return on Total Assets and ROE is Return Equity. ROT, ROTA and ROE are percentage returns of net profit on turnover, total assets and equity respectively.
Source: Author's Own Computations

The return on turnover for the firms reviewed had a mean ROT of 11.89 and a standard deviation of 11.57 for the three years before the privatization, while the mean and the standard deviation of ROT for the three years after the privatization were 15.11 and 9.01 respectively. This shows that the companies performed better after the privatization than before privatization. The deviations of the returns were higher for the period before the privatization than after the privatization. This is an indication of more stable turnover and net profit.

The return on total assets for the firms reviewed had a mean ROTA of 2.94 and a standard deviation of 8.81 for the period before privatization, and the mean and standard deviation of ROTA for the period after privatization were 4.67 and 3.83 respectively. This is an indication that the companies performed better after the privatization and that the deviations in returns were less spread as compared to the period before the privatization.

The return on equity for the period before privatization had a mean ROE of 31.06 and a standard deviation of 39.92. For the period after privatization ROE had a mean and standard deviation of 53.28 and 31.26 respectively. This shows a marked improvement in return for the period after privatization. However, the deviations in the spread of the returns are high in both periods, but higher for the period before privatization.

All the three measures of financial performance showed that the firms performed better after privatization and that they became more stable in that deviation in the returns were - less spread in the period after privatization than before privatization.

4.3 Financial Performance of the Privatized Firms

The various firms which are the subject of this study have been analyzed individually using various performance measures such as return on turnover, return on total assets and return on equity to get the firms' annual performance for the period before and after privatization. This is shown in Table 4.2.

Table 4.2: Firm's Performance on the Basis of Return on Turnover, Return on Total Assets and Return on Equity

Firm	Ratio	Year Prior to Privatization			Year After Privatization		
		Year 1	Year 2	Year 3	Year 1	Year 2	Year 3
	ROT	33	18	16	17	30	15
	ROTA	5	2	2	2	4	2
KENGEN	ROE	61	29	32	44	88	38
	ROT	16	30	16	17	16	17
	ROTA	0	1	1	3	3	3
HFCK	ROE	56	25	14	63	48	52
	ROT	-2	0	6	8	-3	8
	ROTA	-2	0	8	1	-2	9
MSCL	ROE	-14	-3	62	6	-21	78
	ROT	8	4	3	28	9	6
	ROTA	1	1	1	2	2	1
NBK	ROE	94	88	14	37	50	39
	ROT	-9	0	17	8	11	9
	ROTA	-14	-1	33	8	10	7
KQ	ROE	-73	-2	67	37	57	52
	ROT	21	26	11	28	25	23
	ROTA	5	7	3	11	9	9
KEN RE	ROE	33	50	26	99	89	103

Note: ROT is Return on Turnover; ROTA is Return on Total Assets and ROE is Return 011 Equity. ROT, ROTA and ROE are percentage returns of net profit 011 turnover, total assets and equity respectively.
Source: Author's Own Computations

4.3.1 Kenya Electricity Generating Company Limited

The returns on turnover (ROT) for the three years before the privatization are 33, 18 and 16 respectively, while ROT for the corresponding three years after the privatization are 17, 30 and 15 respectively. The return on turnover improved in the first year (2007) after privatization. The improvement was further amplified in the second year (2008). However, in the third year (2009) the performance dropped drastically. On average the performance by the firm for the two periods show no apparent change on the basis of return on turnover. The improvement in return on turnover in the first and the second years can be attributed to the growth in the national economy following the reforms initiated by the Government over the period 2003 - 2007. Other factors which can be attributed to improvement in the performance could be the demand on the management by the board of directors to deliver on the terms agreed on following the listing of the company on the Nairobi Stock Exchange. The fall in performance in the third year (2009) can be attributed to the adverse weather conditions experienced in that year which led to fall in water levels in the dams of the company. Hydro-electric power forms the highest source power generated by the company.

The returns on total assets (ROTA) are 5, 2 and 2 respectively for the three years before privatization, while ROTA for the three years after privatization are 2, 4 and 2 respectively. The return on total assets was low in the first year (2007) after privatization, rose in the second year (2008) but again fell in the third year (2009). Overall, the performance on the basis of return on total assets does not seem to present any significant change for the two periods. The improvement in return on total assets in the second year (2008) can be attributed to the acquisition of more technologically advanced equipment that boosted generation of power leading to higher turnover and net profit. The fall in performance in the third year (2009) can be attributed to the adverse weather condition experienced in that year leading to low turnover and net profit and low return on total assets.

The returns on equity (ROE) for the three years before privatization are 61, 29 and 32 respectively, and ROE for the three years after privatization are 44, 88 and 38 respectively. The return on equity rose significantly in the first year (2007) after privatization and the rise the continued into the second year (2008) but dropped in the third year (2009). Overall, the performance by the company shows a significant improvement after privatization on the basis of return on equity. The improvement in return on equity in the first and the second years can be attributed to the growth in the national economy following the reforms initiated by the Government over the period 2003 - 2007. The fall in performance in the third year (2009) can be attributed to the adverse weather condition experienced in that year leading to low turnover and net profit and hence low return on equity.

4.3.2 Housing Finance Company of Kenya Limited

The returns on turnover (ROT) for the three years before privatization are 16, 30 and 16 respectively, while (ROT) for the three years after privatization are 17, 16 and 17 respectively. The return on turnover improved in the first year (1993) after privatization, slightly dropped in the second year (1994) and again rose slightly in the third year (1995).

On average, the performance on the basis of return on turnover improved in the period after privatization. The company pursued diversification strategy by venturing into ancillary areas of business related to the development and finance of residential houses. The expanded portfolio included: mortgages on commercial properties; insurance; estate management and technical consultancy. These efforts helped to grow the net profit and therefore improved the return on the turnover.

The returns on total assets (ROTA) for the three years before privatization are 0, 1 and 1 respectively, and the ROTA for the period after privatization are 3 for all the three years. The return on total assets improved in the first year (1993) after privatization and remained constant in the second year (1994) as well as the third year (1995). Overall, the performance on the basis of return on total assets is higher for the period after privatization. The diversification strategy meant expanded market and therefore growth in sales and profits. The growth in profit thus improved the return on assets.

The returns on equity (ROE) for the three years before privatization are 56, 25 and 14 respectively, while ROE for the three years after privatization are 63, 48 and 52 respectively. The return on equity improved significantly in the first year (1993) after privatization; however, it dropped in the second year (1994) but again rose in the third year (1995). Therefore the performance on the basis of return on equity shows there is an improvement in the period after privatization. The improved profitability following business diversification resulted in higher returns on the equity employed and thus the probable return to the share-holders.

4.3.3 Mumias Sugar Company Limited

The returns on turnover (ROT) for the three years before privatization are -2, 0 and 6 respectively, while (ROT) for the three years after privatization are 8, -3 and 8 respectively. The return on turnover improved significantly in the first year (2002) after privatization, dropped in the second year (2003) and rose again in the third year (2004) to the level of the first year. On average, the performance on the basis of return on turnover improved in the period after privatization. The improved performance after privatization can be attributed to the management's effort in the strengthening of the distribution network and therefore increasing the market penetration and the company's sugar reached virtually all parts of the country. Also during this period the company branded its sugar and introduced the 2kg, 1kg, 1/2kg and 1/4kg packets to target the various income groups of its probable customers. This effort resulted in improved turnover and net profit.

The returns on total assets (ROTA) for the three years before privatization are -2, 0 and 8 respectively, and the ROTA for the three years after privatization are 1, -2 and 9 respectively. The return on total assets improved in the first (2002) after privatization, dropped in the second year (2003) but rose in the third year (2004). Overall, the performance on the basis of return on total assets does not seem to present any significant change for the two periods. The increased penetration of the market and the expansion of the production capacity meant more investment in assets meaning that the profit would be spread over more assets thus resulting in lower returns on the assets for the first two years after privatization. However, as the gains of the market penetration and capacity expansion start being felt in the third year, the returns on assets improves and this is likely to continue into foreseeable future.

The returns on equity (ROE) for the three years before privatization are -14, -3 and 62 respectively, and the (ROE) for the three years after privatization are 6, -21 and 78 respectively. The return on equity rose significantly in the first year (2002) after privatization and then dropped in the second year (2003) but rose significantly in the third year (2004). Overall, the performance by the firm shows an improvement after privatization on the basis of return on equity. The results of the capacity expansion pursued by the management after privatization were not felt in the first two years thus low returns on equity. However, as the results of the expansion start being realized in the third year, the returns on equity rises and this is likely to continue into the near future.

4.3.4 National Bank of Kenya Limited

The returns on turnover (ROT) for the three years before the privatization are 8, 4 and 3 respectively, while ROT for the corresponding three years after the privatization are 28, 9 and 6 respectively. The return on turnover improved significantly in the first year (1995) after privatization; however this improvement was not maintained as in the second year (1996) the performance dropped drastically and fell further in the third year (1997). However, on average the performance by the company for the two periods on the basis of return on turnover shows some improvement in the period after privatization. The company's management embarked on deposit mobilization by expanding its branch network after privatization. The bank also relaxed its terms for extending loans to its customers. For instance, salaried customers could secure loans by presenting their pay-slips for the last three months. This helped the bank to boost its turnover as well as the net profit.

The returns on total assets (ROTA) for the three years before privatization are 1, 1 and 1 respectively, and the ROTA for the period after privatization are 2, 2 and 1 respectively. The return on total assets improved in the first year (1995) after privatization and remained constant in the second year (1996), eventually dropping slightly in the third year (1997). Overall, the performance on the basis of return on total assets is higher for the period after privatization. The deposit mobilization and the relaxed leading terms together with the strengthening of controls over operational cost helped improve the profit thus improving the return on the assets.

The returns on equity (ROE) for the three years before privatization are 94, 88 and 14 respectively, and the ROE for the three years after privatization are 37, 50 and 39 respectively. The return on equity rose significantly in the first year (1995) after privatization and rose slightly in the second year (1996) but again fell slightly in the third year (1997). Overall, the performance by the firm shows a drop after privatization on the basis of return on equity. The bank increased it share capital by more than one and half times, but the growth in turnover and the net profits did not match the increase in share capital, therefore the lower performance in terms of return on equity in the period after privatization. The increase in assets may reverse this trend as this may help the bank to boost its turnover and net profit.

4.3.5 Kenya Airways Limited

The returns on turnover (ROT) for the three years before the privatization are -9, 0 and 17 respectively, while ROT for the corresponding three years after the privatization are 8, 11 and 9 respectively. The return on turnover dropped in the first year (1997) after privatization; rose in the second year (1998) and dropped again in the third year (1999). However, on average the performance by the company for the two periods on the basis of return on turnover shows some improvement in the period after privatization. After privatization the company embarked on cost cutting measures which involved installation of strong financial and budget processes. These measures included: reduction in the fleet and increase in the utilization of the remaining aircrafts; review of the routes and fares structure and reduction in staff numbers through voluntary severance programme. These measures helped to reduce costs while improving the net profit and thus the growth in return on turnover.

The returns on total assets (ROTA) for the three years before privatization are -14, -1 and 33 respectively, and the ROTA for the three years after privatization are 8, 10 and 7 respectively. The return on total assets dropped in the first year (1997) after privatization, rose in the second year (1998) and then dropped slightly in the third year (1999). Overall, the performance on the basis of return on total assets improved in the period after privatization. The cost reducing measures employed by the management helped improve the net profit and thus improving the return on the assets.

The returns on equity (ROE) for the three years before privatization are -73, -2 and 67 respectively, and the ROE for the three years after privatization are 37, 57 and 52 respectively. The return on equity dropped in the first year (1997) after privatization, rose in the second year (1998) and dropped again in the third year (1999). Overall, the performance by the firm shows an improvement after privatization on the basis of return on equity. The ability of the management to lower the cost through strong financial control and budget processes, helped to grow the net profit which in turn improved on the return on the equity.

4.3.6 Kenya Reinsurance Corporation Limited

The returns on turnover (ROT) for the three years before the privatization are 21, 26 and 11 respectively, while (ROT) for the corresponding three years after the privatization are 28, 25 and 23 respectively. The return on turnover rose in the first (2008) year after privatization, dropped in the second year (2009) and again dropped slightly in the third year (2010). However, on average the performance by the company for the two periods on the basis of return on turnover shows some improvement in the period after privatization. Following the privatization, the corporation embarked on a growth strategy that involved marketing strategies to expand the existing business and acquisition of new business. This helped to grow the premium revenue and therefore turnover. At the same time the corporation employed financial controls to ensure that costs do not grow at the same rate the revenue was growing. The result of these efforts was improved return on turnover.

The returns on total assets (ROTA) for the three years before privatization are 5, 7 and 3 respectively, and the (ROTA) for the three years after privatization are 11, 9 and 9 respectively. The return on total assets rose in the first year (2008) after privatization, dropped in the second year (2009) and remained at the same level in the third year (2010). Overall, the performance on the basis of return on total assets improved in the period after privatization. The growth in net profit as a result of aggressive marketing and the effective cost control measures ensured improved returns on assets.

The returns on equity (ROE) for the three years before privatization are 33, 50 and 26 respectively, and the ROE for the three years after privatization are 99, 89 and 103 respectively. The return on equity rose significantly in the first year (2008) after privatization, dropped in the second year (2009) and rose again in the third year (2010). Overall, the performance by the firm shows an improvement after privatization on the basis of return on equity. The improved net profit following the expanded market and thus revenue ensured the growth in returns on equity.

4.4 Discussion of Results

When the firms reviewed are analyzed using summary statistics such as mean and standard deviation on the performance measures such as return on turnover, return on total assets and return on equity; the firms show improved performance on all the three measures. The means of the returns are higher on all the measures of performance for the period after privatization and the deviations between the returns are lower for the post-privatization period. This is an indication that the firms performed better following privatization and that returns were stable as shown by the low standard deviations on all the three performance measures for the post-privatization period as compared with the pre-privatization period.

When the firms are analyzed individually on the three measures of performance none of the six firms failed to perform better after privatization on all the measures of performance. Only one firm, (Kenya Electricity Generating Company), registered no apparent change on two of the measures of performance i.e. return on turnover and return on total assets. One firm, (Mumias Sugar Company), registered no change on return on total assets. The lack of improvement on the return on total assets could be accounted for by probably the increase in assets following privatization which may have been financed by borrowing rather than by equity. However, National Bank registered a drop on return on equity. Housing Finance Company and the Kenya Reinsurance Corporation registered improvement on all the three measures of performance.

4.5 Summary

Though there were instances where a firm did not show apparent change on either one or two of the measures of performance, none of the six firms reviewed failed to show an improvement on all the three measures of performance used. When all the firms are analyzed as a single unit on all the three measures of performance for the period before and after privatization, using summary statistics such as mean and standard deviation, the performance for post-privatization is higher than that for the pre-privatization. This observation leads to the conclusion that the Government of Kenya should move away from carrying out commercial undertakings and leave this to the private sector for effective utilization of resources and profitability.

CHAPTER FIVE

SUMMARY AND CONCLUSION

5.1 Introduction

This chapter presents the summary, conclusion and the recommendations of the research. Section 5.2 gives the summary of key findings of the research; section 5.3 presents the conclusion of the research; section 5.4 gives the limitations of the research and section 5.5 gives the recommendations for further research.

5.2 Summary of Key Findings

The privatized firms examined by this study had improved performance after privatization. This is shown by the fact that the means on their returns on turnover, total assets and equity were higher for the post privatization period than for the pre-privatization period. The improved performance is further emphasized by the lower standard deviations on the returns on turnover, total assets and equity for the period after privatization than for the period before privatization. The lower deviation in the returns for the post privatization period is an indication of the stability of returns following privatization.

5.3 Conclusion

Overall, the results show significant improvement in the financial performance of the privatized firms after privatization. It is therefore necessary for the Government of Kenya to pursue the privatization policy. The Government should thus move away from pursuing commercial activities and instead concentrate in activities such as human capital enhancing activities, provision of services and creating the legal and institutional framework conducive to increased private investment.

5.4 Limitations of the Study

It is important to note that no partitions were applied especially with regard to the market structures (competitive versus noncompetitive firms), fully versus partially privatized firms and control versus revenue privatizations. A window period of period of three years for the post-privatization was used. This may not be enough to document with no doubt that the firms indeed turned round.

5.5 Recommendations for Further Research

More research on privatization experience in Kenya needs to be done especially to assess the influence of economy-wide changes on the firms' performance. Other avenues of research with regard to privatization experience should deal with the effect of privatization on the development of the stock market in Kenya and other countries in Africa.

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APPENDICES

Appendix (i) List of Firms Reviewed

Kenya Electricity Generating Company Limited

Housing Finance Company of Kenya Limited

Mumias Sugar Company Limited

National Bank o Kenya Limited

Kenya Airways Limited

Kenya Reinsurance Corporation

Appendix (ii) Data on Net Profit, Turnover, Total Assets and Equity

Mumias Sugar Company Limited				
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH.)	EQUITY (KSH.)
1998	-138,862,000	6,186,102,000	8,554,111,000	1,020,000,000
1999	-30,052,000	6,407,988,000	9,252,410,000	1,020,000,000
2000	630,214,000	9,905,072,000	8,232,256,000	1,020,000,000
	YEAR OF IPO			
2002	65,116,000	784,233,000	9,604,112,000	1,020,000,000
2003	-215,608,000	7,628,937,000	9,021,853,000	1,020,000,000
2004	791,451,000	9,792,503,000	9,147,337,000	1,020,000,000
National Bank of Kenya Limited				
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH.)	EQUITY (KSH.)
1991	116,945,000	1,377,337,000	9,687,598,000	125,000,000
1992	109,471,000	2,658,902,000	10,690,526,000	125,000,000
1993	87,685,000	2,799,757,000	12,824,654,000	625,000,000
	YEAR OF IPO			
1995	370,221,000	1,345,752,000	18,256,865,000	1,000,000,000
1996	502,334,000	5,832,282,000	24,447,197,000	1,000,000,000
1997	387,692,000	6,072,902,000	31,090,007,000	1,000,000,000
Kenya Airways Limited				
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH,)	EQUITY (KSH.)
1993	-512,664,000	5,862,486,000	3,754,361,000	700,796,000
1994	-43,434,000	11,141,907,000	3,827,418,000	2,308,077,000
1995	1,539,730,000	9,078,333,000	4,696,220,000	2,308,077,000
	YEAR OF IPO			
1997	851,000,000	10,712,000,000	11,191,000,000	2,308,000,000
1998	1,314,000,000	11,648,000,000	13,392,000,000	2,308,000,000
1999	1,207,000,000	13,225,000,000	17,711,000,000	2,308,000,000
Kenya Reinsurance Corporation Limited				
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH,)	EQUITY (KSH.)
2004	489,156,000	2,303,063,000	8,964,618,000	1,500,000,000
2005	748,170,000	2,866,636,000	10,377,685,000	1,500,000,000
2006	390,449,000	3,544,719,000	11,264,158,000	1,500,000,000
	YEAR OF IPO			
2008	1,481,100,914	5,203,963,000	13,665,599,971	1,500,000,000
2009	1,120,529,000	5,302,203,000	15,000,633,000	1,500,000,000
2010	1,541,391,000	6,729,044,000	17,240,929,000	1,500,000,000

Housing Finance Company of Kenya Limited				
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH,)	EQUITY (KSH.)
1989	11,114,700	71,342,089	2,766,536,000	20,000,000
1990	35,291,790	118,088,379	3,208,765,000	140,000,000
1991	19,884,861	124,309,607	3,435,731,000	140,000,000
	YEAR OF IPO			
1993	144,339,961	830,674,968	4,449,632,731	230,000,000
1994	165,983,356	1,039,859,787	5,346,261,766	345,000,000
1995	180,966,153	1,084,367,690	6,627,945,179	345,000,000
Kenya E	ectricity Generating Company Limited			
YEAR	NET PROFIT (KSH.)	TURNOVER (KSH.)	TOTAL ASSETS (KSH,)	EQUITY (KSH.)
2003	3,347,517,000	10,217,605,000	69,091,745,000	5,495,904,000
2004	1,620,573,000	8,963,074,000	73,867,776,000	5,495,904,000
2005	1,753,152,000	11,011,577,000	77,900,268,000	5,495,904,000
	YEAR OF IPO			
2007	2,445,666,000	14,551,767,000	101,966,861,000	5,495,904,000
2008	4,809,445,000	16,091,563,000	106,993,551,000	5,495,904,000
2009	2,070,913,000	13,559,599,000	102,736,136,000	5,495,904,000

Source: The Firms' Respective Prospectuses/Information Memoranda and their Subsequent Annual Accounts and Reports