FINANCING DECISION IN PUBLIC SECTOR ENTERPRISES : AN EMPIRICAL STUDY OF SELECTED UNITS

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This paper examines the financial structure of selected public sector enterprises. The study shows that the public sector enterprises have adequate sources of funds but large variations can be seen in their utilization of these sources. So, the public sector in itself is not inefficient and there is a considerable scope for improvement, it is essential that the performance of different public enterprises in the area of financing decisions should be carefully evaluated from time to time and corrective measures should be taken if necessary.

INTRODUCTION

The stepping stone must be laid down with utmost care and solidarity, being the foundation of the whole building. Even a single minor mistake would destroy the whole building. So is the case with financing decision, being the first and hence, most important step in the process of financial management of an undertaking.

The financing decision involves a consideration of three principal responsibilities of a finance manager. These are :

(a) Estimation of total financial requirements for the business enterprise,

(b) Identification of sources of finance and determination of financing mix, and

(c) Cultivating sources of finance and raising the required finance.

In other words, it covers two inter-related aspects :

(a) Determination of an appropriate financial/capital structure, and

(b) Raising the required amount of funds.

STATEMENT OF THE PROBLEM

The focus of the present research paper is to review the financing decision of selected public sector enterprises with the view to find out (a) whether the enterprises estimate the financial requirements for long period and short period correctly, and (b) whether the enterprises determine and maintain a desirable combination of various sources of funds. An attempt has also been made to find out the necessary pitfalls in the financing decision of these undertakings and suggest the required remedial measures to make their financing decision more effective and fruitful.

HYPOTHESES OF THE STUDY

The present work will be exploratory and hence, hypotheses based. Certain propositions pertaining to the financing decision of public sector enterprises have been made.

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1. It is assumed that financing decision of public sector enterprises is not satisfactory and not according to the standards prescribed for them. The basis for this assumption is that they emphasize more upon other things like providing efficient services to the customers or upon satisfying public in general.

2. It is further assumed that financing decision of all the public sector enterprises is not uniform in the degree of efficiency. This hypothesis is based upon the observation that some are found to be more efficient while some are found to be less efficient in their financing decision.

3. Efficient financing decision reduces the cost of financing plus optimizes the value of firm. It has been a tried and tested fact.

SCOPE AND METHODOLOGY OF THE STUDY

The present study is confined to Central Government Industrial Enterprises which are engaged in the manufacturing sector. The companies selected for the study represent the industries of steel, minerals and metals, power and petroleum. They are :

1. Steel Authority of India Limited (SAIL)
2. Bharat Aluminium Company Limited (BALCO)
3. National Thermal Power Corporation Limited (NTPC)
4. Gas Authority of India Limited (GAIL)

The study is an empirical one and it covers a period of five years, ranging from 1993-94 to 1997-98. The period has been considered sufficient to reveal the short-term and long-term fluctuations.

For the purpose of this study, both primary and secondary data have been used. For collecting the primary data, a questionnaire was prepared and direct personal investigation method was followed. The secondary data have been obtained from the annual reports of the undertakings and other such records for the relevant period. The data have been analysed by applying various Accounting techniques such as comparative statements analysis and common - size analysis.

FINANCING DECISION OF THE SELECTED CENTRAL PUBLIC SECTOR ENTERPRISES : AN ANALYSIS

The study of financing decision can be made from the point of view of the length for which funds are needed with their respective ownership. As a matter of fact, an enterprise needs funds for financing long-term, medium-term and short-term requirements :

(i) Long-term finance refers to that category of funds whose repayment is not within a period for which tentative business plans can be worked out. The period will vary among various industries. Generally, it is raised for a minimum period of ten years from shareholders, debenture-holders, financial institutions and retained earnings. Such type of finance is used for investment in fixed assets, such as land, buildings, plants, machinery, furniture, fixtures, etc.

(ii) Medium-term/Intermediate-term finance is that category of finance whose repayment can be projected within a planning cycle of reasonable length of time but extends beyond the budget period. It is raised for a period of more than one year but less than ten years from debentureholders financial institutions, public deposits and commercial banks. This type of finance is required for investment in permanent working and for repayment of assets.

(iii) Short-term finance is that category of finance which is employed by an enterprise when the size and nature of funds is such as to generate sufficient cash flow to retire debt within a payment period of one year or less. It is raised from public deposits, trade credit and commercial banks and so represented by current liabilities and provisions. It is invested in current assets because current assets are auto-matically converted into cash during routine business operations. From this cash, short term liabilities are liquidated. It is also known as working capital.

A business firm can raise these funds from two main sources :

(i) owned funds, and

(ii) borrowed funds.

Owned funds refer to the funds provided by the owners. In a joint stock company, funds raised through the issue of shares and reinvestment of earnings are the owned funds. Borrowed funds refer to the borrowings of a business firm. In a company, borrowed funds consist of the funds raised from debentureholders, financial institutions, public deposits and commercial banks.

Now, the long-term sources of these selected units consist of equity shares, reserves and surplus, and secured loans and unsecured loans. The short-term sources include current liabilities and provisions. An analysis of the financial structure of each of the units under study follows.

STEEL AUTHORITY OF INDIA LIMITED (SAIL)

It is clear from the Table 1 that overall, the amount of equity capital has increased from Rs. 3985.89 crores in 1993-94 to Rs. 4130.40 crores in 1997-98. But sharewise in total financial structure, the picture is altogether different. It has been decreasing since 1993-94. It decreased from a figure of 17.82 percent in 1993-94 to 11.90 percent in 1997-98. This is not a very healthy sign. Reserves and surplus have shown an increasing trend all over these years but their share in total financial structure started decreasing from 1995-96 onwards. Their figure increased from 7.94 percent in 1993-94 to 13.75 percent in 1995-96. But from there, it decreased to 12.76 percent in 1997-98 though not much decline. Loan funds of the company have increased from 50.67 percent in 1993-94 to 57.66 percent in 1997-98. Current liabilities and provisions have decreased from 23.57 percent in 1993-94 to 17.68 percent in 1997-98. On the whole, the firm's dependence on borrowed capital had been decreasing till 1995-96 as compared to owned capital. But from 1995-96 onwards, the position has been reverse. The share of borrowed capital started increasing while that of owned capital started decreasing. The owned capital figure decreased from 28.03 percent in 1995-96 to 24.66 percent in 1997-98 while the borrowed capital increased from 71.97 percent in 1995-96 to 75.34 percent in 1997-98. This is a risky affair, particularly, from the point of view of

Table 1 : Financial Structure of SAIL for the period 1993-94 to 1997-98.

(Rs. in Crores)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98
OWNED/SHAREHOLDERS' FUNDS					
Long-term Funds					
Equity Share Capital	3985.89 (17.82)	3985.89 (16.07)	41.30.40 (14.28)	4130.40 (12.95)	4130.40 (11.90)
Reserves and Surplus	1774.91 (7.94)	2649.68 (10.68)	3978.96 (13.75)	4339.09 (13.60)	4427.58 (12.76)
	5760.80 (25.76)	6635.57 (26.75)	8109.36 (28.03)	8469.49 (26.55)	8557.98 (24.66)
BORROWED/OUTSIDERS' FUNDS					
Long-term funds					
Secured Loans	1616.42 (7.23)	2389.85 (9.63)	4381.30 (15.14)	6783.00 (21.26)	8900.68 (25.61)
Unsecured Loans	9714.15 (43.44)	9824.60 (39.60)	10192.31 (35.23)	10638.21 (33.35)	11113.93 32.02)
Short-term Funds					
Current Liabilities	4328.40 (19.35)	4825.05 (19.45)	5212.03 (18.02)	5075.03 (15.91)	5289.58 (15.24)
Provisions	943.90 (4.22)	1134.13 (4.57)	1034.24 (3.58)	935.35 (2.93)	848.59 (2.44)
	16602.87 (74.24)	18173.63 (73.25)	20819.88 (71.97)	23431.59 (73.45))	26152.78 (75.34)
Total Funds	22363.67 (100.00)	24809.20 (100.00)	28929.24 (100.00)	31901.08 (100.00)	34710.76 (100.00)

Source : Compiled from the Annual Reports of SAIL.

Note : Figures in parentheses show percentage of respective item taking total funds/total liabilities as hundred.

long-term stability. Efforts should be made to increase equity and decrease the borrowed component.

BHARAT ALUMINIUM COMPANY LIMITED (BALCO)

A salient feature of BALCO, as depicted in Table 2, has been that its equity share capital remained constant throughout the period under study at Rs. 48885 crores. But, its share in the total financial structure has been on the declining trend all over these years. It declined from 60.16 percent in 1993-94 to 44.72 percent in 1997-98.

Table 2 : Financial Structure of BALCO for the period 1993-94 To 1997-98

(Rs. in Crores)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98
OWNER/SHAREHOLDERS' FUNDS					
Long-term Funds					
Equity Share Capital	488.85	488.85	488.85	488.85	488.85
	(60.61)	(58.87)	(49.73)	(45.02)	(44.72)
Reserves and Surplus	28.98	119.47	268.75	315.12	372.94
	(3.57)	(14.39)	(27.34)	(29.02)	(34.11)
	517.83	608.32	757.600	803.97	861.79
	(63.72)	(73.26)	(77.06)	(74.04)	(78.83)
BORROWED/OUTSIDERS' FUNDS					
Long-term Funds					
Secured Loans	13.28	0.61	-	-	-
	(1.63)	(0.07)	-	-	-
Unsecured Loans	139.30	70.16	59.21	51.85	44.60
	(17.14)	(8.45)	(6.02)	(4.78)	(4.08)
Short-term Funds					
Current Liabilities	97.32	101.90	100.60	101.32	109.18
	(11.98)	(12.27)	(10.18)	(9.33)	(9.99)
Provisions	44.92	49.42	66.20	128.69	77.62
	(5.53)	(5.95)	(6.73)	(11.85)	(7.10)
	294.81	222.09	225.47	281.86	231.40
	(36.28)	(26.74)	(22.94)	(25.96)	(21.17)
Total Funds	812.65	830.41	983.07	1085.83	1093.19
	(100.00)	(100.00)	(100.00)	(100.00)	(100.00)

Source : Compiled from tha Annual Reports of BALCO.
Note : Figures in parentheses show percentage of respective item taking total funds/total liabilities as hundred.

The reason being is an increase in the amount of other components like reserves and surplus and provisions charged. Reserves and surplus have really been increasing at a greater rate. They have increased from a figure of Rs. 28.98 crores in 1993-94 to Rs. 372.94 crores in 1997-98. The loan funds have been substantially reduced by the company by paying them off. The secured loans have been nil from 1995-96 onwards which is a positive improvement in the area of financial structure. In totality, their share decreased from 18.77 percent in 1993-94 to 4.08 percent in 1997-98. Current liabilities and provisions have been fluctuating from 16.91 percent in 1995-96 to 21.18 percent in 1996-97. In brief, the owned capital dominates the financial structure. This is a positive signal to the stability of financial structure of a company and efforts should be made to maintain this dominance of owned capital with increasing trends.

NATIONAL THERMAL POWER CORPORATION LIMITED (NTPC)

Table 3 shows that the company's equity capital has been on the declining trend during the period under study, both amountwise and, particularly, sharewise. Overall, its amount decreased from Rs. 7999.84 crores in 1993-94 to Rs. 7545.78 crores in 1997-98 while its share declined from 30.57 percent in 1993-94 to 24.65 percent in 1997-98. Reserves and surplus have been continuously adding up to the total equity. This is all because of adequate operating revenues. Amountwise, they increased from Rs. 5332.61 crores in 1993-94 to Rs. 10339.21 crores in 1997-98 and sharewise they increased from 20.38 percent in 1993-94 to 33.78 percent in 1997-98. The loan funds have decreased from a figure of 40.85 percent in 1993-94 to 29.15 percent in 1997-98. This shows a wise decision by the company regarding the long-term financial solvency. The performance of the company, in the area of short-term credit, has been fluctuating---increasing, decreasing and then again increasing. All over these years, current liabilities and provisions have increased from 8.21 percent in 1993-94 to 12.42 percent in 1997-98. The company has been certainly making good use of all sources, except long-term loan funds, to finance its assets. This practice has not only increased the margin of safety of the creditors but has also strengthened the financial position of the company.

GAS AUTHORITY OF INDIA LIMITED (GAIL)

After analysing the financing decision of GAIL, as shown in Table 4, one can say that though equity share capital has increased but very late, i.e. from 1996-97 onwards. That, too, is very negligible. The table indicates that equity share capital remained constant at a figure of Rs. 845.32 crores during the entire period of 1993-94 to 1995-96. From 1995-96, it increased from Rs. 845.32 crores to Rs. 845.65 crores in 1996-97. In 1997-98 too, it remained at the same figure of Rs. 845.65 crores while its share in total funds has continuously declined from 26.49 percent in 1993-94 to 11.70 percent in 1997-98. Contribution of reserves and surplus has rather increased from 15.55 percent in 1993-94 to 35.52 percent in 1997-98. The debt capital has also declined from 27.14 percent in 1993-94 to 20.44 percent in 1997-98. Current liabilities and provisions of the corporation have been quite on the increasing trend during these years. It is only in 1997-98, they declined quite significantly. They increased from 30.82 percent in 1993-94 to 43.44 percent in 1996-97. In 1997-98, they dropped to 32.35 percent. Though overall, both owned capital and borrowed capital have been showing a quite fluctuating trend throughout the period under study yet it can be seen that borrowed capital has dominated the owners' funds all over these years. It is a risky sign not only to the adequate margin of safety of the creditors but also, more importantly, to the financial solvency of the concern. So, the management must look into it.

Table 3 : Financial Structure of NTPC for the period 1993-94 to 1997-98

(Rs. in Crores)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98
OWNED/SHAREHOLDERS' FUNDS					
Long-term Funds					
Equity Share Capital	7999.84 (30.57)	7999.84 (29.10)	7334.97 (27.18)	7403.78 (26.57)	7545.78 (24.65)
Reserves and Surplus	5332.61 (20.38)	6327.21 (23.01)	7495.46 (27.78)	8740.90 (31.37)	10339.21 (33.78)
	13332.45 (50.94)	14327.05 (52.11)	14830.43 (54.96)	16144.68 (57.95)	17884.99 (58.43)
BORROWED/OUTSIDERS'FUNDS					
Long-term Funds					
Secured Loans	2957.03 (11.30)	3202.45 (11.65)	3217.13 (11.92)	3272.19 (11.75)	3003.40 (9.81)
Unsecured Loans	7733.30 (29.55)	7371.48 (26.81)	7034.23 (26.07)	6400.31 (22.97)	5919.82 (19.34)
Deferred Payment Liability	-	-	196.24 (0.73)	-	-
Short-term Funds					
Current Liabilities	2080.74 (7.95)	2459.20 (8.94)	1496.58 (5.55)	1533.63 (5.50)	1947.76 (6.36)
Provisions	68.31 (0.26)	134.13 (0.49)	207.26 (0.77)	509.18 (1.83)	1855.47 (6.06)
	12839.38 (49.06)	13167.26 (47.89)	1251.44 (45.04)	11715.31 (42.05)	12726.45 (41.57)
Total Funds	26171.83 (100.00)	27494.31 (100.00)	26981.87 (100.00)	27859.99 (100.00)	30611.44 (100.00)

Source : Complied from the Annual Reports of NTPC.

Note : Figures in parentheses show percentage of respective item taking total funds/liabilities as hundred.

Table 4 ; Financial Structure of GAIL for the period 1993-94 to 1997-98

(Rs. in Crores)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98
OWNED/SHAREHOLDERS' FUNDS					
Long-term Funds					
Equity Share Capital	845.32 (26.49)	845.32 (22.84)	845.32 (17.75)	845.65 (14.01)	845.65 (11.70)
Reserves and Surplus	496.37 (15.55)	813.27 (21.97)	1245.07 (26.14)	1733.57 (28.72)	2568.12 (35.52)
	1341.69 (42.04)	1658.59 (44.81)	2090.39 (43.89)	2579.22 (42.74)	3413.77 (47.21)
BORROWED/OUTSIDERS'FUNDS					
Long-term Funds					
Secured Loans	-	26.93 (0.73)	64.39 (1.35)	117.39 (1.95)	514.33 (7.11)
Unsecured Loans	866.09 (27.14)	778.98 (21.04)	737.68 (15.49)	717.15 (11.88)	963.56 (13.33)
Short-tem Funds					
Current Liabilities	952.44 (29.85)	1185.05 (32.02)	1779.65 (37.36)	2268.65 (37.59)	1567.34 (21.68)
Provisions	30.95 (0.97)	51.93 (1.40)	90.87 (1.91)	352.81 (5.85)	771.59 (10.67)
	1849.48 (57.96)	2042.87 (55.19)	2672.59 (56.11)	3456.00 (57.26)	3816.82 (52.79)
Total Funds	3191.17 (100.00)	3701.46 (100.00)	4762.98 (100.00)	6035.22 (100.00	7230.59 (100.00)

Source : Compiled from the Annual Reports of GAIL.

Note : Figures in parentheses show percentage of respective item taking total funds/total labilities as hundred.

CONCLUSION AND SUGGESTIONS

After analysing the financing decision of all these units, it can be easily inferred that only BALCO has got a quite optimal financing decision with more of owned funds to borrowed funds. Moreover, its owned funds has increased from 63.72 percent in 1993-94 to 78.83 percent in 1997-98. NTPC comes second to it, in having an optimal financing decision, with owned funds increasing from 50.94 percent in 1993-94 to 58.43 percent in 1997-98. All other units have depended too much on borrowed funds. So, they needs to check their financing policies to make them more fair, transparent, and innocuous.

Keeping the above discussion in view, one can say that there is a need to improve the financing decision of some of the units selected for study. It is suggested that :

1. Equity, i.e. external as well as internal must be raised more in comparison of the debt capital. They neither impose any burden on the resources of the undertaking nor they create any charge on the assets of the company.
2. Necessary reserves should be created and build up for future growth of the business. They are the most convenient source of internal financing for a concern.
3. Ceiling should be imposed on raising loans and debt to reduce the dependence on debt capital and avoid any possible insolvency in future.
4. Last, but not the least is that the operating efficiency of each of the concerned undertakings must be toned up. This will help to generate enough revenues not only for meeting the requirements of business but also for building enough reserves for the future contingencies.

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