Methodology for assessment of financial health of state-owned and municipality-owned companies in Ukraine

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Project

The methodology has been created within the initiative "**Promoting transparency and implementation of anti-corruption measures in state-owned enterprises and local governments in Ukraine**". This initiative is being implemented from October 2018 until March 2020 by Ukrainian think-tank the International Centre for Policy Studies (ICPS), in partnership with the Institute for Economic and Social Reforms in Slovakia (INEKO) with the financial support of the Official Development Assistance of the Slovak Republic (SlovakAid). It aims to improve the efficiency of the state administration, self-government and civil society in the area of creation and oversight of regional policies, administration of state-owned enterprises, and monitoring of budgets and information openness of local authorities.

Objective

Improving financial stability of state-owned enterprises through financial analysis tools – INEKO and ICPS will analyze financial indicators of top 50 UA state-owned companies or municipality-owned companies[1], compare them among each other, compare their performance with private sector, and create an interactive portal to display the results for individual companies.

Activities

1. ICPS: Identification of state/municipality-owned companies and data availability check
    Prepare the list of 50 largest state-owned or municipality-owned companies (see note below the line) according to their revenues. Check the availability of financial data required for the financial analysis. The list of data is specified in the "methodology section" below.
2. INEKO+ICPS: Elaboration of methodology for financial analysis of UA state/municipality-owned companies and proposal of financial indicators
    @INEKO: Prepare the methodology and the plan of activities for ICPS. Consult the scope of financial analysis with ICPS. Decide on the final set of financial indicators to be used in the analysis of financial health of state/municipality-owned companies. Suggest the Financial Health Index containing the

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[1] Largest municipality-owned companies will be added to the list in case there is not enough state-owned companies to be analyses.

main financial analysis indicators (the basic set specified in the "methodology section" to enable easy comparison with SK companies).
@ICPS: Propose methodology and further indicators to be analyzed in companies, which are relevant for UA stakeholders, and which goes beyond the basic set of indicators defined in the "methodology section".

3. INEKO: Analysis of financial stability of SK state-owned companies and SK private companies to set benchmark for UA companies
Prepare the financial analysis of selected state-owned companies and selected private companies; the analysis will comprise the same set of basic financial indicators to set the benchmark for comparison with UA companies.

4. ICPS: Collection and processing of UA data & blog (containing general findings from financial indicators of UA state/municipality-owned companies)
@ICPS: Collect financial data required for calculation of financial indicators (from Balance sheet and Profit and Loss statement of companies or from other sources); rewrite them to xls sheet to enable further processing (programming). Use UA data to analyze financial performance of companies and summarize the key findings to a blog article.

5. INEKO: Programming of the interactive web portal with financial indicators of companies
Program the interactive portal containing key financial indicators of UA and SK companies; enable sorting by various criteria and easy comparison of UA and SK companies (state-owned and private ones);

6. ICPS+INEKO: Publication of results, consultations in selected companies, general publicity, blogs
Organize the seminar and prepare the press release to present the key findings from the analysis; publish the blog article; offer companies the individual consultations of their results (max 3 visits).

Timeline

Activity/Month	2018				2019							Responsible
	9	10	11	12	1	2	3	4	5	6	7	
1. Identification of state/municipality-owned companies and data availability check				x	x							*ICPS*
2. Elaboration of methodology for financial analysis of UA state/municipality-owned companies and proposal of financial indicators				x	x							*NEKO+ICPS*
3. Analysis of financial stability of SK state-owned companies vs SK private companies to set benchmark for UA companies						x	x					*INEKO*
4. Collection and processing of UA data, best practices in SK state-owned companies governance, blog (general findings – financial indicators of UA state/municipality-owned companies)						x	x	x				*ICPS+ INEKO*
5. Programming of the interactive web portal with financial indicators of companies									x			*INEKO*

6. Publication of results, consultations in selected companies, general publicity, blog										x		ICPS+ INEKO

Background

Generally, the financial indicators are difficult to read, understand and evaluate. It is the main reason why public and many media representatives are not interested in monitoring or evaluation of performance of the state/municipality-owned companies. The Slovak experience says that if these data are processed and published in easy and understandable way (with the possibility to compare companies' performance data with the reference values) it attracts the public and media attention and increases the pressure on companies to increase their efficiency. The outcomes of this project activity are useful also for politicians who can use them as the source of information for comparison and evaluation of management boards and for evaluation of trends in financial performance of the companies tracking if it is improving or deteriorating.

The way how the public property is managed by state and municipal owned companies affects also citizens' wealth. Ukraine, as any other countries, after declaration of independence has controlled huge stakes in the national economies and it still does. Being fully aware of the risks related to vicious management of state property, we developed this methodology to assess the financial stability of these companies in a more complex way.

Methodology

We will analyze the **balance sheet** (assets and liabilities) and **profit and loss statement** (revenues and costs) of state/municipality-owned companies. We will calculate a **basic set of 10 financial analysis indicators** for each company (figures and indicators are described below).

If relevant, ICPS may suggest extended methodology and further indicators to be analyzed in order to get the broader picture about the overall financial performance of the biggest UA companies.

The basic set of 10 financial indicators will be processed to calculate the overall rating of financial health of companies (calculation of the rating will be prepared by SK experts). The same indicators will be calculated for selected state-owned and private companies in SK (by SK experts) to set the benchmark and enable international comparison of companies. All results will be published on the interactive web page that will enable users to sort companies by indicators or overall rating and will enable them to compare financial health of UA companies with SK ones.

KPIs:

- **50 UA companies** included in the analysis (primarily state-owned; if not enough, we'll include also municipality-owned companies)
- **10 financial analysis indicators** per company
- **10 media releases** related to this part of the project (including **2 blog articles**)
- **1000 views on the portal per Quarter**

Sources for verification:

- Internet – state/municipality-owned companies financial health portal
- Media monitoring
- Stakeholder survey – views of 10 stakeholders to evaluate if the project helps to increase the public pressure on financial efficiency improvements of the companies

Financial Analysis Indicators (the basic set):

Liquidity Ratios	Current Ratio	Current Assets ÷ Current Liabilities
	Quick Asset Ratio	Cash + Marketable Securities + Accounts Receivable) ÷ Current Liabilities
	Cash Position Ratio	Cash ÷ Current Liabilities
Profitability Ratios	ROA - Return on Assets	Net Profit ÷ Total Assets
	ROE - Return on Equity	Net Profit ÷ Equity
	ROS – Return on Sales	Net Profit ÷ Sales
Leverage ratios	Total Debt to Total Assets	Total Debt ÷ Total Assets
	Debt-to-EBITDA Ratio	Total Debt / Earnings Before Interest Taxes Depreciation & Amortization
Activity ratios	Working capital turnover ratio	Net Sales ÷ ((Beginning Working Capital + Ending Working Capital) / 2) Note: Working Capital = Current Assets Minus Current Liabilities)
	Accounts receivable turnover ratio	Net Sales ÷ ((Beginning Accounts Receivable + Ending Accounts Receivable) / 2)

List of required data (for the basic set of financial indicators):

- Total Assets
- Current Assets
- Cash
- Marketable Securities
- Accounts Receivable
- Equity
- Net Profit
- Total Debt

- Current Liabilities
- Sales
- Net Sales
- EBITDA (Earnings Before Interest Taxes Depreciation & Amortization)

Initial activities by ICPS:

1) Prepare the list of 50 biggest state-owned companies. In case there is not enough state-owned companies, add municipality-owned companies to the list to have 50 companies for analysis.

2) Check availability of data; we will need **balance sheet** (assets and liabilities) and **profit and loss statement** (revenues and costs) – two basic accounting reports reported annually. We will need 2017 and 2016 data (note: In Slovakia companies always publish current and previous year data in the latest accounting reports; if so also in UA, there will no need to collect 2016 data separately).

3) Check the structure of data in balance sheet and profit and loss statement. Look at the yellow field in the Financial Analysis Indicators table above – can we identify all required parameters in the accounting reports?

4) Collect accounting reports and re-write raw data to xls sheet for all companies to be processed in the mathematical model of financial health.

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