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Assessment of financial sustainability of the state owned companies

Generally, the financial indicators are difficult to read, understand and evaluate if a person does not have the necessary background. It is the main reason why public and many media representatives are not interested in monitoring or evaluation of the performance of the state/municipality-owned companies. The Republic of Moldova is not an exception and faces the same problems. The Slovak experience says that if these data are processed and published in an 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.

Once the information regarding the economic and financial performance of state-owned companies is published, the decision making circles will have the necessary information to assess the performance of the management teams, while civil society will have the opportunity to put pressure and to hold accountable all the actors involved.

Development of the financial sustainability index

To create the financial sustainability index of state-owned companies, 50 companies with the following features were selected: the assets under management more than 1 million MDL, equity more than 1 million MDL. The companies that have a strategic significance for the national infrastructure have been included in the sample by default. The financial sustainability index consists of 10 indicators, which assess the financial performance, the capacity to face the financial obligations in short and long-term, the liquidity and leverage ratios.

Hence, the index has been formed from the following indicators:

1. **Liquidity ratio** – evaluates the coverage level of current liabilities by current assets. A proportion of 1:1 shows a sufficient coverage of the current liabilities, meaning that the company has the necessary liquidity to face all current liabilities. A level lower than 1, is risky but this doesn't mean that the company will bankrupt. Usually, this indicator is the result of the business model implemented by the company. Companies in industries, such as the retail industry, typically have current ratios below 1. This is acceptable to investors given that these companies are able to negotiate long credit periods with suppliers while offering shorter credit periods to customers. This means that they would have higher account payables, which falls under current liabilities, compared to lower account receivables under current assets.
2. **Profitability ratios** – this indicator is divided into 3 sub indicators: Return on equity, return on assets, return on sales. This ratio shows the performance of the operating activity and the profit margin of the company. The first 2 sub – indicators calculate the profitability of the equity and the assets employed in the operating activity, while the profit margin shows us how much from 1 MDL in sales will end up as profit.
3. **Leverage ratio –** shows by how much the debt is covered with total assets and earnings before interest, taxes and depreciation. If this ratios are higher than 1, it means that the company can face a financial distress risk.
4. **Activity ratio –** show the ability of the company to transform different positions of the balance sheet into cash and cash equivalents. It also shows how efficient is management in employing the assets to generate revenues. A level lower than 1, implies that the company is not run efficiently.

The information on which the index was developed has been collected from the financial statements of the selected companies for 2015-20167 years. On the other side, the colleagues from INEKO collected the same information about Slovak private and state-owned companies in order to set up a benchmark for comparison of Moldovan companies.

Preliminary findings:

1. Out of 50 companies 12 are joint stock and 38 are stated owned;
2. The total revenues of the selected companies is approximately 40 billion of MDL, with assets under management in amount of 74,7 billion of MDL;
3. 12 companies out of 50 suffered losses in the analyzed time period;
4. 7 companies have a volatility of revenues between 20 % and 35%, which is actually creating a major risk for financial sustainability;
5. 7 have a return on equity higher than 15%, 10 companies have a return on equity higher than 5%, the rest of the companies have a ROE below 5%;
6. 4 companies have a profit margin higher than 15%, 7 companies have a profit margin higher than 5%, the rest of the companies have a PM lower than 5%;
7. 3 companies have a return on assets higher than 15%, 4 companies have a return on assets higher than 5%, the rest of the companies have a ROA less than 5%;
8. 2 companies have a leverage higher than 75%, 5 companies have a leverage higher than 25%, 6 companies have a leverage higher than 15%, while the rest of the companies have the leverage lower than 10%;
9. 17 companies have a level of TD/EIBTDA more than 1, which means that the level of debt is higher than the annual EBITDA more than 100%. For example, S.A. Air Moldova have a coefficient of 37.88 of annual EBITDA in order to cover the issued debt; State company State Administration of roads has this coefficient at 1080.71; State company “Mecagro” has this coefficient at 115.26; S.A. “Energocom” has this coefficient at 16.29; State company National Radio Frequencies has this coefficient at 27.85; S.A. “Franzeluta” has this coefficient at 7.81. According to international standards a coefficient higher than 4 or 5 is very dangerous for the company, because it is a very low probability that the company will be able to face its liabilities.

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