PalArch's Journal of Archaeology of Egypt / Egyptology

THE IMPACT OF GOING PUBLIC ON THE FINANCIAL PERFORMANCE OF PETROCHEMICAL INDUSTRY IN SAUDI ARABIA

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Razan Bahauddin H. Maglad, Rozina Shaheen. The Impact of Going Public on The Financial Performance of Petrochemical Industry in Saudi Arabia -- Palarch's Journal of Archaeology of Egypt/Egyptology 18(13), 1199-1206. ISSN 1567-214x

Keywords: Investment, Initial Public Offering, Ipo, Financial Performance Saudi Arabia

ABSTRACT

Going public could have a positive impact on the performance of firms. After the Initial public offering (IPO) process, a company can improve its financial performance and enhance its production. Therefore, this work has examined the effect of IPO on the financial performance of petrochemical companies in the Kingdom of Saudi Arabia. In this work, four companies (3 public and 1 private) from the petrochemical industry were used as sample. The public companies are Petro Rabigh, YANSAB, and SABIC and the private company is SATORP. For this work, financial statements of these companies were used as the data. The financial data were analyzed from the year 2006 to 2018. In addition, financial ratios were used to evaluate the financial performance of a collection of public and private companies. The findings of this work have shown that the public companies (SABIC, YANSAB, and Petro Rabigh) have demonstrated better financial performance compared to the private company SATORP, despite the economic recession. The financial performance of public companies has shown a better performance than that of a private company. This represents the positive impact that the public will have on the financial performance of the company.

CCS Concepts

• Information systems→Database management system engines • Computing methodologies→Massively parallel and high-performance simulations.

INTRODUCTION

Initial public offering (IPO) is an external source of corporate equity [1]. It involves selling part of the company's shares to public investors and becoming publicly listed on the stock market [1]. Before selling the shares of the firm, the company is considered "private" with a small number of investors, such as early contributors (founders, families and friends) and professional investors (venture capitalists) [2]. After becoming a public company, the issued shares are offered to anyone interested in investing in the company and, as a result, the number of investors will eventually increase [2]. Hence, the company is trading on the stock market that allows investors to buy and sell their shares.

Firms have two sources of funding for their business [3]. One is the debt financing of their project and the other is equity. Using debt means borrowing money that needs to be repaid plus interest by issuing bonds to raise money. The other source is external equity, which sells the shares of the company to raise money. Usually this is done through the IPO [3]. In order to initiate an IPO, the issuer or the company that goes public shall give the investment bank or the underwriting firms the authority to value the company [4]. Valuation of the company helps to determine the price of the stock, the best type of security to be issued, the number of shares and the best time for trading the stock [4]. Thus, the investment bank or the underwriting firms determine all of these, which is the due diligence necessary to evaluate the company before it is made public [5].

The process of making a company public is a long process that usually takes 6 months and more to be done [5]. There are several steps that a company must take in order to be publicly listed, which are bank selection, filing and due diligence, pricing, stabilization and transition [6]. The decision to go public is one of the most important decisions any company can make [6]. There are many reasons to go public, but the main reason is to raise funds, which is the main advantage that can be gained through this procedure. Some companies go public in order to increase their market position over their rivals [7]. When the company becomes public, it collects additional market shares over its competitors [7]. When the firm is public and this gives the shareholders the ability to diversify risk and gain greater variability in profits than the owners of private companies [8]. Firms that go public increase their capital expenditure, sales, total assets, fixed assets and profitability compared to the year before the IPO [8]. This means that companies that want to increase their investment scale or adopt more risky market strategies to improve their market position tend to decide to go public [8].

The impact of IPO on the financial performance of companies has been studied previously in a number of academic reports. Zattoni et al. [9] examined the role of the board members in the financial performance of the IPO-listed firms and found that, following the IPO process, the role of the board member was very important in monitoring and enhancing the financial performance of the firm. Guldiken et al. [10] analyzed the impact of media coverage on IPO finance performance and found that the inclusion of the IPO firm in valid capital related media has a fundamental impact on its stock cost and pricing. Schwieterman et al. [11] assessed the impact of the supply chain on the post-financial performance of the IPO list firm and found that the post-IPO financial performance of the firm is significantly related to the company's supply chain structure. Huang et al. [12] analyzed the effect of financial market development on IPO stock pricing and found that firms located in better-established financial markets have been experiencing less undervaluing and better performance as a result of higher market simplicity.

The petrochemical industry plays a key role in the Saudi financial account, as changes in oil prices usually directly affect the balance of the Saudi account [13]. In addition, when the global price of oil is declining; Saudi Arabia's revenues are also declining, which is causing both an account and a budget deficit. The decision to publicize any petrochemical company is therefore very sensitive to the Saudi economy. Successful IPO will enhance and improve the Saudi economy and, conversely, failure to implement the IPO will risk negatively affecting the Saudi economy. Thus, this work was done to analyze the subject of initial public offering (IPO) and its effects on the financial performance of petrochemical companies in the Kingdom of Saudi Arabia.

METHODOLOGY

Quantitative research method has been used for this work. The sample population of this work consisted of four companies from the petrochemical industry. Of the four companies, three are publicly listed and one is private. The public companies are Petro Rabigh, YANSAB, and SABIC and the private company is SATORP. The source of data used is Tadawul, which is the Saudi stock trading market, and companies' website. The data used is extracted from the financial statements of these companies. The period of the financial data of the companies that were analyzed is between 2006 to 2018. Furthermore, financial ratios were used to evaluate the financial performance of a collection of public and private companies. The performance of these firms was evaluated using the most commonly used indicators of firms' performance; return of assets (ROA) and return of sales (ROS), current ratio and fixed asset turnover.

The first financial ratio is return on assets which measures the efficiency of asset exploitation, as shown in Equation 1.

$$Return\ on\ assets = \frac{Earnings\ before\ Taxes}{Total\ Assets} \times 100 \quad (1)$$

The second ratio is ROS which is used to evaluate the companies' operational efficiency, as shown in Equation 2.

$$Return\ on\ Sales = \frac{Earnings\ before\ Taxes}{Sales} \times 100 \quad (2)$$

The third ratio is the current ratio, which demonstrates the ability of the company to fulfill its short-term obligations by using its short-term asset. It is one of the liquidity measurements as shown in Equation 3.

$$Current\ Ratio = \frac{Current\ Assets}{Current\ Liabilities} \quad (3)$$

The fourth and last financial ratio is the Fixed Assets Turnover. This ratio measures how efficiently company's fixed assets are used to generate sales, as shown in Equation 4.

$$Fixed\ Asset\ Turnover = \frac{Sales}{Fixed\ Assests} \quad (4)$$

RESULT AND DISCUSSION

Analysis

Figure 1 represents ROA for the four companies. Based on Figure 1, Petro Rabigh's return of asset is improving after its IPO. Where it declined due to the economic recession and decrease in the oil price in 2014, then it began improving again in 2015. SABIC and YANSAB ROA increased after they became public which is in 2010. Their decline is tied with the decrease in the oil price. SATORP ROA has a great increase from 2014 to 2015 because it started its commercial operation, which is moving in the opposite direction of all other three companies. SABIC and YANSAB obviously have performed better than SATORP throughout the whole period.

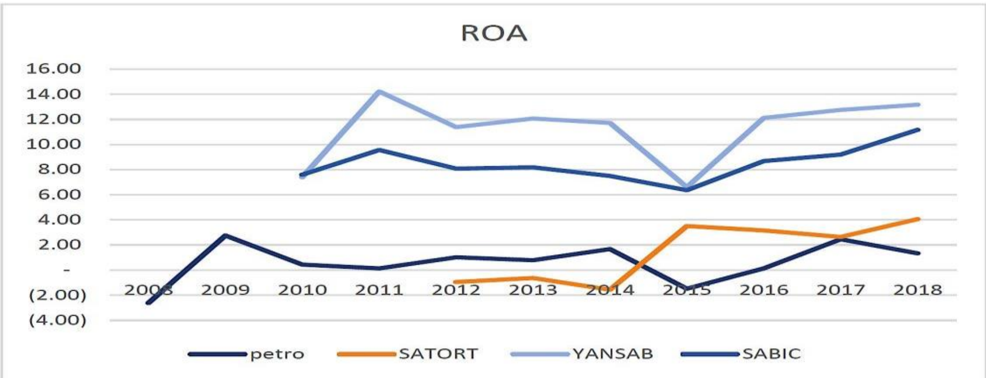

Figure 1. Return of Assets (ROA)

Figure 2 represents the ROS for the four companies. Based on Figure 2, the results showed that public firms' ROS is almost moving opposite than SATORP's ROS. Furthermore, YANSAB and SABIC have a higher ROS than SATORB. Likewise, SABIC, YANSAB and Petro Rabigh are more affected by the economic recession. In addition, the other two companies SABIC and YANSAB have return on sales more than SATORP even during the economic recession and both performed much better.

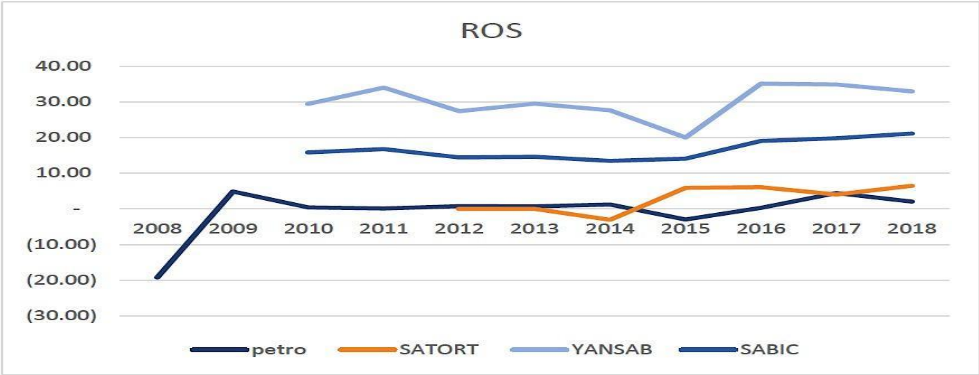

Figure 2. Return of Sales (ROS)

Figure 3 represents the current ratio for the four companies. Based on Figure 3, public firms have a better current ratio than SATORP even during the recession that has occurred in the economy. This means that SABIC, YANSAB and Petro Rabigh's short-term liquidity is better than SATORB, which is more capable of fulfilling their short-term obligations than SATORP.

Figure 4 represents the fixed assets turnover for the four companies. Based on Figure 4, the overall performance of the public companies is better that the private company (SATORP). This means public firms tend to be better than the private firm in managing their fixed asset investment to generate earnings in the long term.

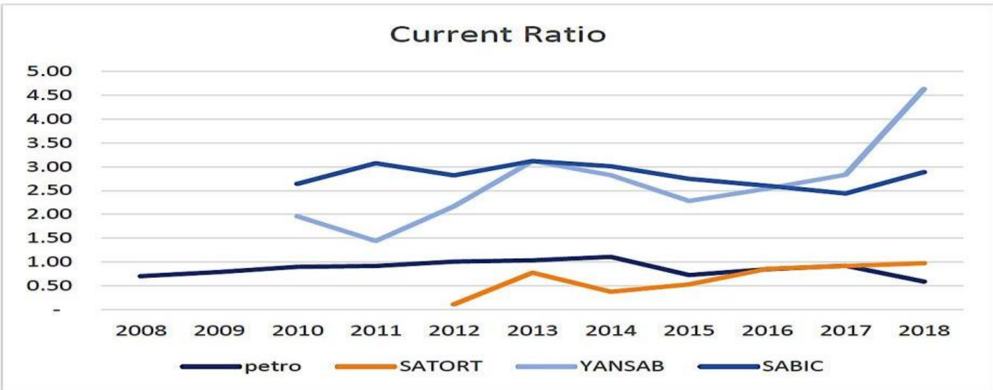

Figure 3. Current Ratio

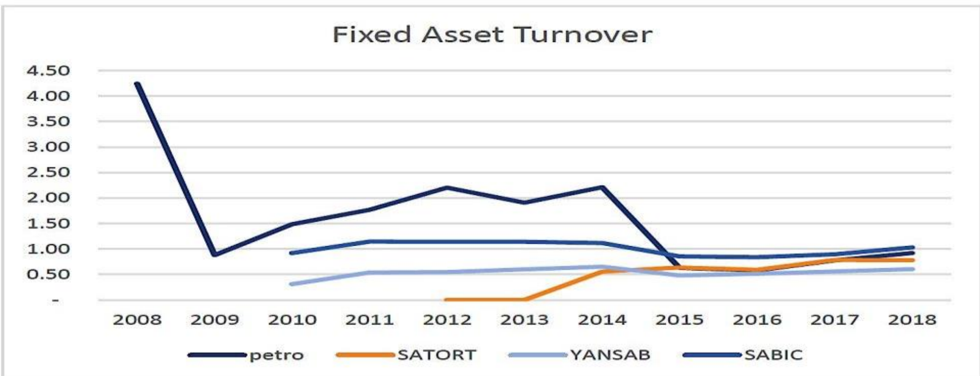

Figure 4. Fixed Asset Turnover

To clearly identify the impact of going public on the performance of private company, the evaluation measurements of firms' performance which are ROA, ROS, FAT and Current Ratio were conducted. This evaluation applies the ratios on SABIC company before and after going public during 2008-2013 and for Petro Rabigh the period between 2006-2011 (examining 3 years of before being public and 3 years after going public). The average of the ratios of 3 years before IPO and 3 years after going public was calculated. Table 1 shows the result for SABIC company. Based on Table 1, SABIC's ROA before it was made public was lower than public. Also, SABIC has the same Current Ratio, FAT when it's public and private. However, after the IPO, SABIC ROS is lower than when it was private.

Table 1. SABIC Company

Indicators	SABIC Pre-IPO	SABIC After IPO
ROA	4	8
Current Ratio	1	1
ROS	19	15
FAT	1	1

Table 2 shows the result for Petro Rabigh company. Based on Table 2, for the Petro Rabigh company, it has higher ROA and ROS when they are public. Furthermore, its Current Ratio and FAT are the same before and after the IPO. After analyzing Petro Rabigh and SABIC before and after going public, it can be observed in general that both companies perform better or have the same performance after becoming public compared to when they were private.

Table 2. Petro Rabigh Company

Indicators	Petro Rabigh Pre-IPO	Petro Rabigh After IPO
ROA	0	1
Current Ratio	1	1
ROS	5	1
FAT	2	2

OVERALL DISCUSSION

After assessing the performance of public and private petrochemical companies by using certain financial ratios, the effects of going public on the financial performance of the companies were deduced. Applying the profitability ratios ROA and ROS to public and private firms shows that public firms have better ROA than private firms. The return on assets of public firms is moving at the price of oil, unlike the private company. The increase in the ROA is the result of an increase in the price of oil, which directly increases the sales of public petrochemical companies. On the other hand, in the case of a decrease in oil prices, the sales of public companies are negatively affected, unlike the private ones as the private companies are moving on opposite direction of oil price movement. Furthermore, the results have shown that public firms have a better liquidity ratio than private firms, which is more than 1. In addition, the liquidity of most public firms is increasing over the years. This may be due to a decrease in the portion of the long-term loan. Public firms may reduce their debt by using equity to finance their activities. This improves the company's current ratio. In addition, according to the Fixed Asset Turnover, public firms are also moving in the same direction as oil price movements. Thus overall, it is deduced that that public companies are able to demonstrate better performance than private companies. The outcome of this work, is in accordance to the work of Mburugu et al. [14] and Piloto Sincerre et al. [15] where it was confirmed that public firm have a better financial performance after the IPO process, which is beneficial to the company in the long run.

CONCLUSION

This research paper has summarized the impact on petrochemical companies when they decide to change their status from private to public. In this regard, the impact of IPO was analyzed by a demonstration of 4 real-life mega companies that dominate the majority of the petrochemical industry in Saudi Arabia. Overall, public companies have achieved higher profitability ratios between ROA and ROS compared to private firms. In addition, the financial performance of public companies appears to be strongly influenced by the global price of crude oil, and their revenue trend is directly in line with the oil price trend. To sum up, public companies (SABIC, YANSAB, and Petro Rabigh) have shown better financial performance compared to the private company SATORP.

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