"Financial Analysis of Karnataka Power Corporation Limited Accountability Based On Demand"

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Abstract:

Analyze the performance of Karnataka's power sector. Analyze the financial management practices of Karnataka Power Corporation Limited (KPCL) Identify the problems associated with the financing and investment management practices of Karnataka Power Corporation Limited. Examine the efficiency of asset-liability management practices and ascertain its financial impact on Karnataka Power Corporation Limited. Suggest ways and means of improving KPCL's financing and investment practices to enhance the overall efficiency and profitability of the organization and make comparative analysis with peer corporate.

The study proposes to test the following hypotheses: Professional leadership will render KPCL's financial management practices effective Political interference affects KPCL's financial management practices Inefficiency of the regulator, namely KERC, affects KPCL's financial management practices The study is descriptive in nature and has used the 'fact-finding' survey method. Primary data has been collected by administering Interview Schedules to the respondents. Industrial consumers of power in and around Bangalore city and KPCL personnel drawn from all functional areas of KPCL constitute the sampling universe. Interview Schedules were administered to 100 industrial consumers and 100 personnel of KPCL. Probability sampling in the form of simple random sampling was applied because every industrial consumer and every staffer of KPCL stood an equal and independent chance of being selected. "Nothing moves without power and power does not move without finance[1]".

[1]Source: http://www.scribd.com/doc/50530593/kpcl

Financial Analysis of KPCL :

Power or energy, is a core sector item. Power *empowers* developing countries. If one traces the growth achieved by the advanced economies, one will realise that power enabled them to fast forward their economic growth. Even in South Asia or for that matter South-East Asia, we find countries like South Korea overtaking the much larger economies like China and India on various parameters owing to their well-developed power sector, amongst other things. For example, Karnataka produces around 9,600 megawatt (MW) of power but South Korea that has half of Karnataka's population produces a whopping 64,000 MW!

At the international level, India is among the least producers of power: it produces 1.5 lakh megawatt compared to 8 lakh mw by China and 11 lakh mw by USA[2]. Hence power is an area that an emerging market economy (EME) like India has to focus on in a sustained manner whatever the difficulties it may face along the way. It may be recalled that one of modern India's best engineers and the modern-day Karnataka's chief architect Sir M Visweswarayya remarked, "Industrialise or Perish". None could have put it so succinctly. If Karnataka has to industrialise, it has to rev up the power sector failing which its economy will perish.

Statement of the Problem

It is no secret that India is an agrarian economy notwithstanding the fact that the contribution of agriculture, the economy's primary sector, to the GDP of the country has fallen to 14.5 percent, according to latest estimates. Paradoxically, the sector still keeps 58 percent of the country's population employed.

Scope of the Study

The study covers only the central public sector undertakings

[2] Source: http://bangalorebuzz.blogspot.com/2010/04/dark-ages-for-silicon-plateau.html, accessed on Jan 24, 2012

Scope of the Study

The study confines itself to the Karnataka power sector in general and the Karnataka Power Corporation Ltd in particular.

Objectives of the Study

The objectives of the study are to:

1. Analyze the performance of Karnataka's power sector.
2. Analyze the financial management practices of Karnataka Power Corporation Limited (KPCL)
3. Identify the problems associated with the financing and investment management practices of Karnataka Power Corporation Limited.
4. Examine the efficiency of asset-liability management practices and ascertain its financial impact on Karnataka Power Corporation Limited.
5. Suggest ways and means of improving KPCL's financing and investment practices to enhance the overall efficiency and profitability of the organization and make comparative analysis with peer corporates.
6. **Methodology of Research**
7. The study is descriptive in nature and has used the 'fact-finding' survey method. Primary data has been collected by administering Interview Schedules to the respondents.

8. **Sampling Plan**

9. Industrial consumers of power in and around Bangalore city and KPCL personnel drawn from all functional areas of KPCL constitute the sampling universe.

10. Interview Schedules were administered to 100 industrial consumers and 100 personnel of KPCL.

Sources of Data and Data Collection

Data required for the research has been collected from both primary and secondary sources. Primary data has been collected from the respondents, viz., industrial consumers and KPCL personnel.

Interview schedules specially designed for the purpose were used to collect the said data.

In addition, the Researcher has interacted extensively with the other stakeholders associated with the power sector, notably trade bodies like CII, FICCI and FKCCI to elicit their views and comments on the topic under study.

Secondary data has been collected from reputed journals, magazines, newspapers, annual reports and house journals of KPCL, KPTCL, ESCOMS and house journals of industry bodies like FICCI and CII.

- ✓ Bothe the CAGR figures are unimpressive, to say the least. While the set-back in respect of thermal power generation may have been caused by disrupted coal supplies which are often beyond the government's control, there is no excuse for the under-performance in respect of power generated from other sources. It only shows that the requisite thrust is absent in respect of power generated from other sources and this is unfortunate. This is not the kind of luxury an acutely power-starved state like Karnataka can afford. Investments should be channelled into other sources of power at least by promoting the right type of investment climate for potential investors.

- ✓ Higher levels of current ratio, namely, 5.10, 7.44, 3.72, 4.33, 1.23 and 7.60 respectively for the fiscal years 2005-2010 only indicate that KPCL has not been able to manage its inventories tightly; nor has it managed to wangle better credit terms from its suppliers. In fact there have been instances of corporates like HUL clocking a better current ratio by in turn clocking a negative working capital position! Bankers in India consider the norm as 1.33 although internationally it is 2. KPCL's high levels of current ratio smack of poor financial management particularly considering that in theory at least, it is not saddled with slow-moving inventories. It is time KPCL focused on tight inventory control.

- ✓ Higher levels of quick ratio, namely, 4.71, 6.81, 3.46, 4.05, 1.12 and 7.21 respectively for the fiscal years 2005-2010 confirm the inference drawn from current ratio – poor inventory management and by extension poor financial management has led to this state of affairs. It is time KPCL controlled its inventories more aggressively. A cent-per-cent conservative inventory control policy will hurt the corporation severely.

- ✓ The fluctuation in gross profit margin, from a low of 9.44 percent to a high of 16.65 percent suggests that there is something fundamentally wrong with the way KPCL generates and vends power. This implies that operational costs have been rarely optimal and mostly sub-optimal. The swing in net profit margin to a high of 9.98 from a low of 6.16 during the fiscal years 2005-2010 tells more or less the same story. The two margins indicate that tight and consistent cost control practices are yet to become a permanent feature in KPCL. The corporation should put in place tight and consistent cost control practices to smooth out the fluctuations in gross profit margin and net profit margin.

- ✓ The low levels of fixed assets turnover and total assets turnover ratio point to inadequate exploitation of fixed assets in particular and all assets in general on the part of the corporation. KPCL's return on assets and earning power tell the same story. Being asset-based ratios, the same remedy is relevant if KPCL's return on assets and earning power are to improve. KPCL should improve its operational efficiency. Superior human resources, state-of-the-art capital equipments and superior expertise / knowhow alone can effect a turnaround in the matter. The turnover ratios have to be far better in a capital-intensive industry like power generation. Presently the ratios give the impression that KPCL is saddled with capital equipments based on obsolete technology and human resources short on expertise / knowhow. Considering the kind of capital that has gone into fixed assets, the earlier KPCL acted in the matter, the better.

- ✓ RoE, in percentage terms, of 10.57, 12.06, 7.01, 8.03 and 10.08 respectively for the fiscal years 2006-10 may not interest the equity shareholders anymore considering that even savings bank (SB) accounts with commercial banks generate a return of 6 percent per annum these days. What is more, no uncertainty characterises investment in SB accounts! It is time KPCL tweaked its operations and financial management in line with what has been suggested in the previous paragraphs so the equity shareholders are better rewarded.

- ✓ A stitch in time saves nine and it is something the government will do well to remember. If the government had invested in the power sector as and when the demand-supply mismatch occurred, the yawning gap that one notices now in the mismatch may have been avoided. It is not that the mismatch would have evaporated but at least it would have been within manageable limits. Even the periodic outflows towards investment would have been well within the government's budgetary grasp. Now things have gone too far and hopefully the government has learnt its lesson. It is time that the government improved the investment environment by fine-tuning the policy appropriately because its own coffers are empty. This is possible only by actively working with the Central government as explained in one of the following paragraphs.

- ✓ It is not the government's business to be in business. Hence it should at least ensure that its power sector corporations like KPCL, KPTCL and ESCOMs operate like commercial entities. It should make a beginning in this direction by ensuring that professionals head these institutions and not IAS officers who are better at heading government departments. Fortunately, the country is brimming with capable professionals of proven experience and if the government promises a generous compensation, it can attract the best talent to head its power sector corporations. Simultaneously it should ensure that the heads of these corporations are granted full functional autonomy. This will ensure that political interference is minimised if not eliminated and operations are optimised. It will also ensure that KPCL is held accountable for supply of quality power.
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- ✓ Government should abjure populism if it is serious about saving the power sector. Populism may benefit the government of the day in the short term but will boomerang on it harshly sooner rather than later. Almost all the political parties which have ruled the State or the country for that matter will agree with this statement. They have realised the hard way that sowing the wind will lead inevitably to reaping the whirlwind. The right way to conserve power and reduce its wastage is by pricing it correctly. Correct pricing has ensured conservation of scarce commodities and scarce resources across the world.

- ✓ Proactivity on the part of KPCL could have made things easier in the State's power sector. It could have undertaken construction of mini hydel projects at smaller dams that cater to areas surrounding the dams. With 38 new irrigation projects coming up in the state, it would have mitigated the power crisis. With professional leadership missing, KPCL has let go of this opportunity to mitigate the power crisis. If a seasoned professional had headed KPCL, this opportunity would not have gone unutilized.

- ✓ On occasions, the government of the day does wink at power theft and gets away with it. This is because the regulator, namely, the KERC has not been adequately empowered by the powers that be. On the pretext of footing the bill for power supplied to rural IP sets the government often ends up extending political patronage to vested interests who have a field day. Also, by blaming 'unidentified thieves' many insiders pilfer power and conveniently escape punishment. Other populism-driven but loss-inflicting measures include politicians using their clout to provide power connection to those who do not qualify for it and preventing KPTCL from severing power connection in cases where the bills have not been settled. These nefarious activities can be put an end to if the powers that be empower the regulator, namely the KERC, adequately. It is strongly recommended that the government attend to the task of empowering the regulator on top priority.

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