VENTURE FIRMS IN TRANSITION

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Venture firms and the stock market

Kosdaq-listed venture firms are currently undervalued compared to their performance. In 2000, operating and normal profitability of Kosdaq venture firms were 7.0% and 5.9% respectively, higher than the 3.9% and -3.7% of all Kosdaq-listed firms. Kosdaq venture firms are also safer than other Kosdaq-listed firms in that they have lower debt ratios. However, the price-earning ratios of Kosdaq venture firms fell below those of all Kosdaq-listed firms since January 2001. This was due to remaining investor anxiety about venture firms.

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☐Overall performance

Looking at performance in 2000, Kosdaq-listed IT firms maintained solid performance amid rumors of a venture crisis and the fall in stock prices. Sales growth continued to be strong at 61.5%, despite worries that the firms lacked profit models. The IT firms had debt ratios less than half that of Kospi-listed manufacturers, as well as interest coverage ratios that were twice as high, indicating good stability and soundness.

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Meanwhile, operating profitability and normal profitability for sales were 4.7% and 2.2% respectively, a far cry from their levels in 1999. This is thought to be the result of higher advertising expenditure and sales costs, lower stock values, and exchange rate losses.

Table 1. Performance of Kosdaq-listed IT Venture Firms (survey of 56 firms)

(unit: %)

		1998	1999	2000
Growth	Sales Growth Rate	13.5	57.2	61.5
Profitability	Sales Operating Profitability	10.1	10.2	4.7
	Sales Normal Profitability	4.3	10.5	2.2
Stability	Liquidity Ratio	1.4	2.9	2.5
	Debt Ratio	1.8	0.5	0.7
Soundness	Interest Coverage Ratio	2.2	1.9	2.2
	Current Liabilities/Sales	0.4	0.3	0.3

Source: Financial Supervisory Service, Analysis of Listed Firms, Spring 2001.
Note: Interest Coverage Ratio = Operating Profit/Interest Expenses

□Performance by Industry

Industries that performed good or excellent performance in 2000 included: computer and Internet software and solutions, IT equipment and components, and semiconductor and computer components and materials.

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The computer and Internet software and solutions industry showed strong sales growth and profitability due to public and private investment in digitalization. However, profitability fell from 1999s level due to higher costs from large scale hiring, a higher share of low-margin products (foreign companies occupy most markets for high-margin products), and low market barriers resulting in greater competition.

The IT equipment and component industry saw increased sales due to expansion of high-speed networks and upgraded investment in mobile telecom services. Although profitability was higher than in other industries, operating and normal profitability for sales decreased from the previous year due to higher financial costs, dependence on imported components, and exchange rate losses.

Despite sagging demand for computers, the semiconductor and computer component and material industry saw sales growth of 30%, but sales have decreased since the second half of 2000. Although profitability is comparable to that of IT venture firms, it has worsened from 1999 due to intensifying price competition, exchange rate losses, and fixed costs such as facilities and wages.

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The Internet service and multimedia equipment industry experienced a fall in profitability. The sales growth rate for Internet services fell to one-fourth of that in 1999, and profitability has decreased. Factors in the disappointing profitability include weak sales, excessive advertising expenses, and asset valuation losses.

□Performance by Size

Overall, IT venture firms showed strong management performance but there was some polarization for profitability and soundness depending on the firm's size. In 2000, large IT ventures had sales operating profitability and normal profitability of 7.2% and 5.5% respectively, while interest coverage ratio was very healthy at 3.2. However, smaller IT ventures continued to have negative profitability and their corporate soundness worsened. A factor in the negative profitability of smaller ventures was the excessive cost burden of advertising and office rental.

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Growth and stability was strong for both large and small companies. The sales growth rate for large and small companies were 72% and 30.1% respectively, due to market growth and continuous development of profit models.

Table 2. Performance of IT Venture Firms by Size

(unit: %)

		Kosdaq-listed IT Venture Firms (56)					
		Large Ventures (28)			Small Ventures (28)		
		1998	1999	2000	1998	1999	2000
Growth	Sales Growth	10.8	77.9	72.0	19.1	16.9	30.1
Profitability	Sales Operating Profitability	10.2	8.1	7.2	10.0	16.3	-5.0
	Sales Normal Profitability	4.5	10.9	5.5	4.1	9.3	-10.7
Stability	Liquidity Ratio	1.3	2.6	2.2	1.4	4.0	4.3
	Debt Ratio	1.9	0.6	0.8	1.6	0.4	0.5
Soundess	Interest Coverage Ratio	2.1	3.5	3.6	2.5	1.1	-1.9
	Current Liabilities/Sales	0.5	0.3	0.3	0.3	0.3	0.3

Comments and Prospects

The basic reason for the Kosdaq's plunge was anxiety about less profitable Internet and IT-related companies, and the lack of sound profit models. This anxiety added to jitters about a "venture crisis" that were widespread in September and October 2000, and affected the entire Kosdaq market. However, considering that Kosdaq-listed IT ventures showed strong performance in 2000, the crash of the Kosdaq index in March 2000 was due to oversensitivity by market participants. In particular, the computer and Internet software and solutions industry, as well as the IT equipment and components industry, have shown solid growth and management.

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However, the economic slump of the first half of 2001 is expected to dampen growth and profitability due to decreased IT investment, stagnant semiconductor and PC market,and intense competition.

Although sales growth in the Internet services industry decreased from 1999's figure, the sales growth for 2000 was 114%, which indicates that doubts about profit models were excessive. In the Internet services industry, brand recognition through market occupancy is crucial, and the resulting advertising costs have slashed profitability. However, because small Internet service firms will be less able to sustain poor performance, large firms are expected to dominate the market. In addition, profitability is expected to improve in the reconfigured market, with higher sales and lower advertising costs. VIP

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