Chapter - II

REVIEW OF LITERATURE

The review of literature provides the basis for the study and gives a direction in which the study has to be pursued. Hence various aspects of privatisation was reviewed though the literature survey. This review has covered the following aspects.

i) Ownership Vs. performance
ii) Privatisation Models
iii) Performance of privatised companies.
iv) Post privatisation effect.
v) Indian experience.

OWNERSHIP VS. PERFORMANCE

Prof. Raja Chelliah in his article titled "Privatisation, Planning and market discipline" argues that it is high time that the issue of privatisation is considered pragmatically and not ideologically. The bottomline is efficiency of resource use and not who owns an enterprise. The resource crunch is a crucial factor for governments decision making in the shift from public to private sector. There is, a basic need for market discipline and market discipline can't be wholly ensured under public enterprise. The author marks the difference in divergence between planning and market mechanism, on the one hand, and between the public and private sectors, on the other. The government, perhaps, absent mindedly, says the Professor, went in to areas in production originally not intended for it. It must shed these activities, he pleads. The presentation suggests the creation of a compact and efficient public sector while privatising the inefficient segment.
Prof. S.L. Rao, Director General, National Council of Applied Economic Research, New Delhi in his paper "Ownership, Control And Management Of Public Enterprises" argues that with the power of the Board of Director being extremely limited in both, the author does not find any basic difference in the nature of control between public and private enterprises. The separation of ownership and management has been ineffective in both the cases. The real difference, according to him, is in the commitment, which exists only in private enterprises. The root of the problem of public enterprise performance is to be found in the character of ownership with the state interfering too much in management functions. This has resulted in misguided technology acquisition, poor location decisions, heavy social and welfare responsibilities and concealed costs. MOU, to the author, is a good instrument to spell out the commitment on both sides. The author does not see any point in privatisation of monopoly enterprises. Probably, a dose of private ownership and listing on the stock exchange could help.

John. B. Goodman and Gary. W. Loveman of Harvard Business School in their article titled "Does Privatisation Serve the Public Interest?" say that privatization is like mergers and acquisition: the real issue is managerial accountability, not the form of ownership. They have come to three important conclusions.

1. Neither public nor private managers will always act in the best interests of their shareholders. Privatization will be effective only if private managers have incentives to act in the public interest, which includes, but is not limited to efficiency.

2. Profits and the public interest overlap best when the privatized service or asset is in competitive market. It takes competition from other companies to discipline managerial behaviour.
3. When these conditions are not met, continued governmental involvement will likely be necessary. The simple transfer of ownership from public to private hands will not necessarily reduce the cost or enhance the quality of services.

Prof. V.V.Ramanadham in "Privatisation – a global perspective" concluded thus. "There is an unmistakable and genuine enthusiasm in most countries for privatization. The concept is being implemented, rightly through both divestiture and non divestiture options. The pace of action is, however, behind the expectations of policy framers and implementors themselves. This is not surprising, in view of the complex issues surrounding successful privatization. Two simple caveats may be sounded: first, that the focus ought to focus steadily on efficiency gains as a result of privatization, rather than on divestiture per se; and second, that no divestiture should be so conducted as to contain the seeds of tensions which will trigger a reverse action of some kind in the near future".

Bob Rowthorn and Ha-Joon Chang, in their study, titled "public ownership and the theory of the state" published by Routledge in 1993 (page 65) concluded "In our view the question of public enterprise efficiency can't be divorced from politics. Such efficiency depends on the attitude of the state towards items like competition and budgetary policy, which in turn depends, above all, on the ability of the state to insulate itself against conservative pressures from both inside and outside these enterprises. Where the state can insulate itself adequately, public enterprise may be every bit as efficient as private enterprise, whilst offering additional economic and social advantages. Where the state can't insulate itself, privatization may well lead to greater efficiency, but this can't be taken for granted since the same conservative forces previously at work under public ownership may continue to influence state policy even after privatization."
PRIVATISATION MODELS

In the international workshop on comparative Advantage of Enterprise Models and Privatisation held in New Delhi organised with the technical cooperation of Inter-regional Network on Privatisation, division for Global and Interregional programmes United Nations Development Programme (UNDP) in 1991, many papers on privatization were presented by experts. These papers were edited by Dr. S.R. Mohnot in the publication titled Privatisation-options and challenges.

Prof V.V. Ramanadham in his article titled 'Comparative Advantage of Enterprise Models – A Conceptual Analysis', points out that an enterprise, organised in whatever sector, possesses comparative advantage. The comparative advantage reflects itself in the performance efficiency. The paper pleads for the adoption of comparative advantage as the guiding principle of policy decisions on organization models. It contains that a (financially) losing organisation is not essentially the one which has lost the competitive advantage. Privatisation to the author is a three-pronged concept it can be achieved through ownership, organisation or operational changes. The comparative advantages has two dimensions: financial returns and social returns. Operationalizing comparative advantage is difficult in activities where only public sector operates. Situation like this call for simulation.

Dr. M.B. Athreya in his article titled "Alternative Models of Privatisation or People-isation" examines the issue of privatisation in its basic organisational frame work, with special reference to the role of state in economic activity. It compares parallel concepts of people-isation, degovernmentalisation and marketisation. The author sees the justification of privatisation in the context of its distancing from political and administrative control, accountability, organisation, employee interface and flexibility in operation. He evaluates
different types of intervention towards privatisation: government majority (51% plus), government controlled (51% - 49%), Joint Sector (26% + 25% + 49%) and total privatisation. The emphasis is on ownership aspect in distinguishing the forms of organisation one from another.

Dr. S.R. Mohnot, Executive Director, Centre for Industrial & Economic Research, New Delhi in his paper on 'Enterprise Models-Operationalising Comparative Advantage', attempts to conceptualise the enterprise models and their comparative advantage in the context of privatisation. Six basic issues have been raised: the delimitation of enterprise models in a operative context, identification of parameters of comparative advantage, yardsticks to measure the parameters, mechanisms to tackle non-quantifiable ones, aggregation of the heterogeneous co-efficient and modalities for the application of the measurement to the identified parameters. It focuses on transformation which the enterprise models are encountering.

Professor Nickwoodward in his paper "The underlying assumptions public and private sector models in the UK" briefly reviews the political background to the nationlisation (and denationalisation) programmes in the UK where the debate has focussed on ownership as a critical variable. It suggests that underlying the political discussion of performance are approaches which exclude significant aspects of organisational functioning and behaviour. It concludes by an interrogative: what conditions are necessary to facilitate appropriate performance by enterprises in non-competitive product-markets, publicly or privately owned? The paper concludes with a quote from the Pope "For forms of Government let fools contest; what is best administered is best". The analysis attempts to establish that the performance of organisations is not correlated with the forms of organisation as it is with work culture it creates and fosters. Whether 'culture' can be changed with or without
ownership and how easy it is for an organisation to transform itself, are vexed questions.

Dr. Eamonn Butler, Director Adam Smith Institute the presented paper on Restructuring Public Enterprises at the Indo-British Seminar on International Experiences in Restructuring Public Enterprises held at Administrative Staff College, Hyderabad in March, 1994. According to him, there are ten specific factors which make practical achievement of restructuring a reality and one can see them in examples from all over the world.

1. Delineate the enterprise
2. Corporatize the enterprise: have clear management, clear objectives, clear budgeting, clear accounting.
3. Devolve the management: The most important way to motivate people is to let them take their own decisions and to suffer the consequences or take the reward.
4. Buyout old commitments
5. Introduce incentives
6. Identify and overcome opposition.
7. Adjust the work force.
8. Allow the enterprise to function: provide funds and train the staff towards customer orientation.
9. Do the easy ones first.
   Select small enterprise to reform first, learn the problems and let the process grow larger.
10. Privatize

Dr. Sherry M. Stephenson principal administrator, Trade Directorate, Organisation of Economic Co-operation and Development OECD, Paris, appraises in his paper titled "International Experiences with privatisation", the
major experiences on privatization attempted globally in more than 50 countries. It points out that the experiences are as varied as are objectives. The concept of privatization may sound simple, its successful realisation is a fairly complex process. Bringing into bold relief major characteristics of privatisation in different countries, the paper highlights the problems faced by the British experiment along with its achievements. In developing countries, the paper notes, most of the privatisation efforts focus on asset sales. In Latin America, a few countries achieved perceptible results. Mexico allocated the proceeds generated towards investments in infrastructure and education while Brazil and Argentina used the funds for debt reduction. Pakistan's programme has met with some initial resistance from workers but moves ahead. Malaysia has registered significant progress. Where capital markets are relatively small, contends the author, the privatisation programme shall have, of necessity, to be gradual.

PERFORMANCE OF PRIVATISED COMPANIES

David Parker, professors Keith Hartley and Andrew Dunsire of the university of York conducted a research on “ownership, organisational changes and performance”. This research was funded by the Economic and Social Research Council as part of its Management in Government Initiative (Project no. E 0925006). The outcome of this research appeared in the International Journal of Public Sector Management, vol 5, no.1 (Parker 1992). This research was concerned with (1) testing the hypothesis that a change in organisational status leads to a change in performance, and (2) attempting to identify the relationship between performance and organisation’s internal environment. The result confirms that public to private shift is associated with improved performance, but that this performance improvement is not guaranteed. That the
link between organizational status and performance is apparently much more complex than many commentators (notably politicians) have assumed.

Three conclusions are drawn by the study is that, First, the results appear to be congruent with aspects of organizational theory literature, especially contingent theory, which suggests that performance is the product of many and often subtle forces.

Second, in some cases changes in the internal environment occurred independently of the status change.

Third, where the structure of management changed, the direction of movement was usually towards a more decentralized, profit centre or holding company structure. This accords with the organisational theory literature which suggests that a more decentralized structure is optional when the external environment becomes less stable following the ownership change.

Last, it has long been recognised that the internal environment needs to be congruent with external environment.


The study identified three main effects of privatization: finance, information and control. On finance, the articles has concluded that privatization has only modest effects. The same shift in burden of financing between consumers and investors could have been achieved by raising consumer prices under public ownership.

The capital markets have not been primary source of external finance and wider share ownership has not altered its structure of capital markets in any substantial way. In regard to information, greater transparency has been argued to be an important benefit of privatization. The association of performance with identifiable corporate entities is an important source of incentive. Share prices do provide information on performance that is relevant in setting incentives.
Mathew Bishop and David Thompson in their study titled "Privatisation in the UK – Deregulatory reform and public enterprise performance" have set out the picture of reform of the 1979 public sector that took place during 1980s. According to the study,

First, it is clear that economic performance improved during the decade across the 1979 public sector. If you accept that the central goal of the reforms was to increase the efficiency of the public sector, then the reforms must be judged a success.

Second, improvements in performance were more significant in companies operating in comparative markets or where the introduction of greater competition – through de-regulation or tendering – was feasible. Performance improvement, although positive, was less impressive in the natural monopolies. Ownership change, too, can't be easily linked to changes in performance. Indeed many reforms to companies whilst still under public ownership, by replicating the conditions and pressures observed in the private sector, inevitably reduced the scope for a clear connection between privatization and performance.

In terms of equity, the major casualty of the 1980s public sector reforms was in employment – and that predominantly in certain traditional industries undergoing fundamental structural reform, in particular coal, steel and rail.

POST PRIVATISATION EFFECT

Christos Pitellis and Thomas Clarke who conducted many studies on privatisation said in the concluding remarks of their article titled "The political economy of privatisation" published by Routledge in 1993 (page 25),

"The status and role of public enterprises has been profoundly questioned by the advocates of privatisation. In some countries, including the UK, the political rush to privatize neglected the opportunity to develop competition and made more difficult the effective regulation of the privatized companies. This diminishes the
likelihood of the achievement of major efficiency gains promised at the
time of privatization. Evidence is now emerging of the performance of
the privatized enterprises in the medium term, which suggests that
some significant gains in efficiency have been attained. The extent to
which such improvements in efficiency were based on restructuring
carried out prior to privatization, or were due to reductions in service
or quality of products, or asset sales, is not entirely clear”.

"The question of whether any short and medium term efficiency gains are
sustained for any length of time remains an open one. Anyway, the frequent
intervention of the regulators has clearly been a crucial factor in maintaining the
responsiveness of the privatized monopolies to customer concerns. Anxieties
concerning the behaviors of privatized monopolies supplying vital utilities to the
public have not been entirely assuaged “.

Trefor Jones in his study on “privatization and market structure in the UK
Gas Industry” published by Routledge in 1993 concluded (Page 122)
The failure of government policy towards British Gas which placed the main
emphasis upon privatization without paying much attention to the subsequent
market structure and the development of effective competition. The result was a
failure to achieve the expected results of privatization in that competition failed
to develop and the newly privatized monopoly abused its market power in its non
regulated activities thus attracting considerable criticism of the privatization
process.

V.V.Ramanadham in ‘Privatization and After - monitoring and
regulation’ published by Routledge says,
"The lesson that UK offers, on the whole, is that there should be an
effective, wide ranging public policy in favour of competition, which
obviously subsumes the institution as a surrogate, where necessary.
Surely this is more difficult than introducing adhoc pieces of
regulation, particularly, because the national economies of developing
countries are, in varying degrees, highly prone to monopoly yet.
Policies of liberalization are being initiated, no doubt, but the real impacts of the policies are in the future.

Alzira Salama of Cranfield School of Management, Cranfield University in his study on "Privatisation: Implications for corporate cultural change" published by Avebury (P-128) concluded that change in ownership did not necessarily bring organisational change directly. Rather, the increased competition, deregulation of the market and leaders new values are the factors which trigger culture changes in the organization. Career management, although not responsible for provoking culture changes alone, is revealed as playing an important role in reinforcing new managerial attitudes, and, consequently, gradually reshaping the corporate culture.

INDIAN EXPERIENCE

Sunil Mani in his study titled "Divestment and Public Sector enterprise Reforms – Indian Experience since 1991", published in Feb 1997 observed that, "In most developing countries privatisation or reform of the PSEs has become an inevitable consequence of the structural adjustment programme. India too has followed, a policy of privatisation or more specifically a policy of divesting off governments shareholding in a number of enterprises under its ownership. But this policy has been poorly articulated and its implementation very lackadaisical in nature. Consequently very soon the government is going to be left with a number of poorly performing enterprises which will be a drag on its budget while the better performing and dividend paying enterprises would have left its fold. He argues further that at the root of this apparent contradiction is the real reason behind the reform process in India. Divestiture is thought of primarily as a mechanism to generate non inflationary form of resources to fill in the burgeoning fiscal deficit of the Central Government. Improving performance has been the least of considerations".

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G. Ganesh in his book titled "Privatisation in India" published by Mittal publications - 2001 has concluded that privatization will succeed only if it is conceived as a part of the overall liberalization process, involving removal of protection to inefficient industries in the public sector, amendments to laws which hinder competition, reforms aimed at opening up hitherto closed sectors of the Indian economy and rapid reform of the financial sector. These measures would help considerably in increasing investment for creation of better living standards of the people.

The review of literature shows that, no study has been undertaken to analyse the 'privatisation maturity profile of India', taking into consideration competitive market conditions, regulations, political aspects, capital markets, stock exchanges, managerial capabilities of private sector and macro economic conditions. Another important deficiency is that, the studies conducted so far have not extracted the valuable experience, views and opinions of cross section of the society. The eminent, experienced personalities in politics, government, management, academics and economics have not been probingly interviewed to arrive at right conclusions and to make appropriate suggestions. The causes for the failure of disinvestment policies of the various Governments is not analysed. None of the studies have suggested an Indian model of privatisation based on British and global experience. Hence this study mainly focuses on these areas to make a valuable contribution to the process of privatisation in India.
HYPOTHESES

Based on the framed objectives and review of literature, the following hypotheses are arrived at:

H -1. THE ROLE OF THE GOVERNMENT INTERVENTION IN THE ECONOMIC DEVELOPMENT OF A COUNTRY IS NEED BASED.

H -2. PRIVATISATION IS NOT A PANACEA FOR ALL THE ILLS OF THE PUBLIC SECTOR.

H -3. PRIVATISATION MODEL IS COUNTRY SPECIFIC.