Chapter - I

INTRODUCTION

In the 20th century, state intervention in the economic development of a country has been accepted as a pre-requisite by developed, developing and communist countries alike. In developed countries of Europe, till today the state has a major stake in many industries. In case of developing countries, like India, the state has become an inseparable part of the economy. Even though in many communist countries (i.e., centralised economies) the role of the state is substantially reduced, but till today these countries depend on the state for active participation in the development of its shattered economy. Hence the subject of the state intervention is a global phenomenon.

Since 17th century the role of the state in economic development has been a debatable issue. In 17th century, Adam Smith advocated a limited role for the state. He did not suggest any state intervention in the economic development. The role was that of maintaining law and order. This role remained stagnant till 1920s. In 1920s, Keynes actively advocated for the state intervention due to economic depression and market failures. This argument became more pronounced after the second world war. The shattered economy of many countries cried for state intervention for economic development. Hence nationalisation became well accepted economic policy in many developed countries and developing countries alike.

During the same period a few countries like Russia, East Germany, China and others followed the pattern of central economy which was influenced by the thinking of Karl Marx, Lenin and others. In case of developing countries which were facing problems of inadequacy of capital, lack of market competition, low technical expertise, huge population and poverty, lack of basic infrastructure like drinking water, roads, education etc were forced to accept the state intervention
as the only way out. Hence the state enterprises went on to occupy 'commanding heights' and the state enterprises became 'temples of economy'.

By the turn of the century, sweeping changes had occurred in various fields all over the world which necessitated a re-look at the state intervention in the economic development. Geographically, USSR and East Germany do not exist; centrally controlled economy failed to deliver the goods; cold war is in cold storage. Technological development has made the world a global village. Liberalisation, privatization and globalisation (LPG) is the order of the day. 'Hand holding' by State Government has become a 'hand binding' in the economic development. Public sector units have become a burden to the exchequer. Governments can no more bear the losses out of public money and it has to discharge many other important obligations to the down-trodden. Very often it is said that Government has no business to do business.

Privatisation has become the buzzword in the economic and political world for the last two decades. The pace of privatisation in Britain created international wave of privatisation. Rolling back the frontiers of the state is the policy of many governments around the world. The mood of many governments can be summed up in the words of the champion of privatisation, Margaret Thatcher, the former Prime Minister of the UK. In her own words, as written in her biography "Margaret Thatcher – the Downing Street Years" (p-676)

"Privatization, no less than tax structure, was fundamental to improving Britain’s economic performance. But for me it was far more than that: It was one of the central means of reversing the corrosive and corruptive effects of socialism. Ownership by the state is just that - ownership by an impersonal legal entity: it amounts to control by politicians and civil servants; and it is a misnomer to describe nationalization as the labour party did, as 'public ownership'. But through Privatization – particularly the kind of privatization which leads to the
widest possible share of ownership by members of the public - the state's power is reduced and power of the people enhanced."

In case of India, a developing country with poor infrastructure, and grappling with the problems of unemployment and poverty, the huge investment in public sector has become a great burden for the economy. Many attempts made by the government to disinvest have failed. Hence there is a need to study all the facets of privatisation and to suggest privatisation model for India.

NEED FOR THE STUDY

There are 243 Central Government undertakings with investment of Rs. 2,04,050 crores as on 31st March, 1998 excluding railways, banks, insurance and posts. Out of 243 undertakings, only 10 top enterprises (out of which 5 are in power sector) have investment of Rs. 98,280 crores. Apart from this, there are many public sector enterprises in State Government having investment of Rs. 25,000 crores. The majority of this investment is in power and transport sector. The total investment in public sector undertakings (departmental and non departmental) is Rs. 2,50,000 crores.

As per the analysis of sickness by BIFR, 69 central and 92 state PSUs are registered under SICA as sick industries up to 31st December 1998. Out of 69 central PSUs in which references has been registered, 22 cases were such where rehabilitation schemes were approved/sanctioned by the Board, while in 10 cases winding up had been recommended to the concerned High Court.

Public sector units both at the central and state which were sick numbered 228 with net worth of approximately Rs. 7170 crores, the total accumulated losses of all the undertaking is over Rs. 17,255 crores and the number of workers involved is over 7.56 lakhs.

Since 1990, the successive governments in India are making efforts through various policies to disinvest. All these attempts have failed miserably due to various reasons. Now it is high time. If the government does not apply the political will required, then the country has to face a major economic crisis.
This study conducted in the light of the above situation, does a critical analysis of the privatisation concept, policies and methodologies followed by British in particular and global experience in general. The study takes in to account the causes for growth and fall of public sector in India and analyses the efforts of the disinvestment and its failures. On the basis of various studies made, the study finds out whether India is ready for privatisation or needs to be prepared for privatisation. On the basis of the findings, an Indian Model of Privatisation is proposed to be suggested.

STATEMENT OF THE PROBLEM:-
Privatisation is a complex process. It has many facets. Few important problems one has to consider in case of India are enlisted below.

1. **Investment:**
   The investment in central and state PSUs is huge in size i.e., Rs. 2,50,000 crores. For a developing country like India, which has limited resources this is a very big investment.

2. **Return on Investment:**
   228 units are loss making having accumulated losses of Rs. 17,255 crores. Even in case of profit making units, profit is earned by administered prices like petroleum products.

3. **Deficit Budgets:**
   The governments at centre and state are having deficit budgets and hence they are not in a position to financially support loss making units. Government is diverting its precious resource to support the loss making units instead of investing in infrastructure development like providing drinking water, roads, education and other social obligations.

4. **Employees:**
   Before taking any decisions, the government has to think about providing life supporting systems to displaced employees. PSUs being the biggest
provider of jobs in the country employ 196 lakhs of employees. Out of which, 7.56 lakh employees are in sick units.

5. Policies and Methodologies to Privatise:
The Government has neither formulated any long term policies nor decided over various methodologies for privatisation. Committees are formed and dissolved. Politicians and bureaucrats are totally confused.

6. Political Will:
The government lacks the political will to privatise. Hence it has failed in creating an atmosphere of confidence.

7. Capital Market:
India has small capital market to mobilise the resources required for privatisation. Foreign equity investment is restricted hence required funds don't flow in to the capital market.

8. Regulatory Authorities:
India is not known for quality of regulatory authorities. Hence unless regulatory authorities discharge their duties diligently and honestly privatisation can't succeed. It leads to exploitation of customers and investors.

9. Macro economic conditions:
India has unfavorable macro economic conditions. With a population more than 100 crores, poverty estimates of 354.8 million people, unemployed being estimated (for 95-2000) at 106 million and with per capita income of $ 390, India has a daunting task and hence privatisation process should be well planned.

OBJECTIVES OF THE STUDY:
The major objective of the study is to resolve many empirical issues, intellectual doubts and moral uncertainty developed about privatisation. To provide an up to date reassessment of the theory of practice of privatisation; to offer analysis of
the extent of the competition and efficiency achieved by privatisation. However, more specific objectives of the study are:

- To provide comparative study of privatisation in different countries, with a particular emphasis on the dramatic transformations which have occurred in Britain;
- To provide an up to date assessment of Indian experience with public sector and experiments with disinvestments;
- To explore the myths about private sector;
- To explore the role and potential effects of regulatory agencies;
- To study whether India has the context and circumstances, politically and economically to privatise its public sector;
- Finally, to evolve an Indian model for privatisation taking in to consideration its regulatory agencies, political and economic conditions.

RESEARCH METHODOLOGY

Research Methodology depends on the nature of the subject of the research. The subject understudy is historical in nature as far as pre and post privatisation effects in Britain and is a current topic as far as India is concerned. This data is collected from various secondary sources. Desk research consists of reference to various publications of books, reports, and such other data on British privatisation. British Council Library at Bangalore, was an important source for the study apart from the libraries of Indian Institute of Management at Bangalore Staff Administrative College at Hyderabad and Karnataka University, Dharwad. Various reports published by World Bank, Government of India, Reserve Bank of India, Disinvestment Commission, contributed substantially for the research. Websites of Stock Exchanges helped to give the current reports.
SECONDARY DATA COLLECTION:
To collect the secondary data, the desk research consisted of the following.
1. Paper publications from the period of 1993 to 2001. The facts, figures, views, experience, policies published in Economic Times, the Hindu, the economic & business magazines of India and abroad.
2. Various important publications involving in-depth analysis of the global phenomenon of privatisation as well as regional trends.
3. Proceedings of seminars, symposia and conferences held on the topic of privatisation.
4. The reports of many committees formed for disinvestment in India including Disinvestment Committee’s reports.
5. The report of World Bank, International Monetary Fund and International Finance Corporation on Privatisation.
6. Data relating to stock market, capital markets, regulatory authorities.
7. Data available on various websites including that of London stock exchange.

PRIMARY DATA COLLECTION:
Purpose of collecting the primary data was to gather the opinion of the people who have relevant experience and knowledge in the field of public and private sector.
In case of Britain, privatisation is a history but in case of India, it is a current, burning topic which has to take in to consideration views of the select sample before any findings are arrived at and suggestions made. The two well accepted primary data collection methods i.e., Mail Survey and Interview method are applied to get the best possible results. The details of which are as follows.
Mail Survey (Questionnaire)

The mail survey method of collecting primary data was followed for the following advantages of the method.

Respondents selected were educated and were capable of understanding the objective of the study. Most of the executives/ businessmen/ Academicians/ professionals who responded could not be met personally due to constraint of time and resources. The questionnaire was administered on all India basis keeping in view the balanced regional representation. Mail survey also provided required anonymity and confidentiality. Respondents could complete the questionnaire at their convenience. The responses are expected to be totally free from interviewer bias.

Sampling Method:
The study has followed non-probability sampling technique. The method followed is purposive or Judgement sampling. In this study, a sample selected for administering questionnaire has to have relevant knowledge and/or experience of having exposed to the field of public sector or private sector. Hence on the basis of researcher’s Judgement a purposive sample is selected.

The sample selected for administering questionnaire has the following population.

- **Professionals**
  Chartered Accountants, company secretaries, cost accountants management professionals.

- **Public Sector executives**
  Persons who had served in the capacity of executives and were having the experience of the of public sector management.
• **Private Sector executives**
  Executives who had served in the capacity of executives and were having experience of the Private Sector management.

• **Businessmen**
  Businessmen having exposure to Public and Private sector management culture.

• **Chamber of Commerce and Industries**
  Chamber of Commerce and Industries situated in various parts of the country.

• **Universities and Academic Centers**
  Heads of the department of Commerce of various universities and faculties of Management Institutions.

Geographically, the sample covered various parts of the country. Respondents are from the North, the South, the East and Western parts of the country. Questionnaire is responded from Gujarat, Mumbai, Punjab, New Delhi, Kashmir, Kochi, Ichalkaranji, Kolkata, Hyderabad, Bangalore and various other places.

### Analysis of respondents profile

<table>
<thead>
<tr>
<th>Category</th>
<th>No</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Businessmen</td>
<td>9</td>
<td>12</td>
</tr>
<tr>
<td>Professionals</td>
<td>18</td>
<td>24</td>
</tr>
<tr>
<td>Academicians</td>
<td>17</td>
<td>22</td>
</tr>
<tr>
<td>Public Sector Executives</td>
<td>14</td>
<td>19</td>
</tr>
<tr>
<td>Private Sector Executives</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Institutions/Others</td>
<td>10</td>
<td>13</td>
</tr>
</tbody>
</table>
Analysis of Statewise Responses.

<table>
<thead>
<tr>
<th>State</th>
<th>No</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Karnataka</td>
<td>30</td>
<td>40</td>
</tr>
<tr>
<td>Gujarat</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>11</td>
<td>15</td>
</tr>
<tr>
<td>New Delhi</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Andhra Pradesh</td>
<td>6</td>
<td>8</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Punjab</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Kerala</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>West Bengal</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Goa</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Orissa</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>75</td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Sample Size:
Sample size consisted of 200 samples. 75 responses were received with a response rate of 37.5%.

The Questionnaire:
The Questionnaire was divided into three parts. Each part mentioned the topic head and objective of that part clearly on the top. Each part had close and open ended questions. Close ended questions had three options for ticking the response i.e., yes, no, undecided. Open ended questions gave the option of
freely expressing the views of the respondents in their own words. The questionnaire is reproduced in the Annexure along with the request letter to respond for the questionnaire.

Processing of data:
The data collected had two parts: close ended and open ended Questions. Close ended questions were ticked. (Yes, No, Undecided). The tabulation of this was done by hand tabulation

<table>
<thead>
<tr>
<th>Question</th>
<th>Tally Mark</th>
<th>Number of respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Yes No Undecided</td>
</tr>
<tr>
<td></td>
<td></td>
<td>No</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Undecided</td>
</tr>
</tbody>
</table>

Pie Charts
On the basis of tabulation, the number of respondents and the percentage of respondents was arrived at and pie charts were drawn to give graphical view of the response for each question and sub question.

Open ended Questions
The response to open ended questions were studied and summarised under broad heads to have uniformity of the responses.

INTERVIEW METHOD
For the collection of data, apart from questionnaire method, interview method was also selected because the subject of the study has many qualitative aspects like decision making process in public sector, experience of public sector or private sector management and political aspects of public sector. Interview method will give an opportunity to a highly placed authority to express his/her view in explicit terms. Any person with vast experience in the field would like to
do justice for a subject as complicated as privatisation of public sector undertaking and no piecemeal, half-hearted approach is liked by such personalities.

Sample
Sample for interview was picked up meticulously. Sample consisted of eminent personalities having rich experience. Interviews were recorded on a audio cassette. Reproduction of exact transcription runs in to big volume. Hence, only relevant brief transcription is produced. Persons interviewed were as follows.

1. Ministers and politicians having the experience of the large and medium scale industry.
2. Bureaucrats occupying the positions of chief secretary, finance secretary, commissioner of industry and commerce and others.
3. Chairman and Managing Directors of leading public and private sector undertakings.
4. Professors of management from leading Institutes and economists.

RESEARCH DESIGN:
Research has been designed to cover all facets of privatisation. Research Design takes into account voluminous data - secondary as well as primary data as explained above - and it is presented under various chapter heads to arrive at the right findings and conclusions. The outline of the thesis is as follows:
The First chapter is introductory and gives an overall view of privatisation. It also covers the need for the study, statement of problem of the study, research objectives, research methodology, research design and concepts used in the study.

The Second chapter reviews the literature to present the summary of various studies conducted on British privatisation and Indian experience of disinvestment. The gap in the existing body of knowledge is identified and the need for this study to contribute to the body of the knowledge is explained.

The Third chapter presents the historical and global perspective of state intervention and privatisation. It covers the views of economists like Adam Smith, Keynes, Hayek, Alchian and Demsetz. Privatisation objectives and methodologies are presented to give a total picture of the process of privatisation. Apart from this, the summary of the experience of various countries on privatisation and the methodologies followed is covered to prove that privatisation is a global phenomenon.

The Fourth chapter focuses on British Perspective of state intervention and privatisation. It covers a wide area of nationalization, criticism of public sector, privatisation drive of Margaret Thatcher, pre and post privatisation effect on select 10 companies, problems of privatisation of natural monopolies and lessons to be learnt from British privatisation.

The Fifth chapter concentrates on the Indian perspective. It covers the origin, rise and fall of public sector, the sickness and problems of public sector, various reports on disinvestment - Rangarajan committee, the Disinvestment Commission, the Disinvestment Ministry, BALCO case & Supreme Court Judgement and latest scorecard on disinvestment. The MOST IMPORTANT Part of this chapter is pre privatisation maturity profile of India based on various studies conducted. It covers the report of World Bank, Business study and Coopers & Lybrand, Kay & Thompson, UTI Institute of capital markets, international Finance Corporation and other sources. The study has presented
detailed analysis on certain important parameter of privatisation - market conditions, political conditions, pre privatisation maturity profile, sector wise rating, efficiency of capital markets & stock exchanges, regulatory authorities, characteristics of Indian private sector and macro economic conditions of India.

The Sixth chapter covers the results of the primary data conducted through Mail Survey and Interview Method. In case of Mail Survey, Pie chart has been drawn for each close ended question which gives graphic view of opinion expressed by the respondents. Responses to open ended questions have been summarised. In the interview method, audio recording of all the interviews is summarised and the opinion in brief is given.

The Seventh chapter includes findings and suggestions. A detailed finding on the basis of the study is enlisted. Suggestions are made for successful privatisation in the Indian context in the backdrop of the British and global experience. A graphic presentation of the Indian model suggested is given. The Indian model for privatisation is called as 'Macro Micro Matrix- An Indian model for privatisation.'

CONCEPTS USED IN THE STUDY:

- **Public sector undertaking or state owned enterprise (SOE)**
  An undertaking which is owned by the Government.

- **Private Sector Undertaking**
  An undertaking which is owned by private individuals or a company or group of companies owned by private investors.

- **Joint Sector Undertaking**
  An undertaking whose ownership of the organisation is in the hands of government and private sector.
- **Public Limited Company**
  A Joint stock company with Limited Liability.

- **Privatisation**
  Sale of shares or assets of the public sector undertaking to the private sector to effect the transfer of ownership from public to private sector.

- **Deregulation**
  Removal or Loosening of government restrictions on the pricing, output and investment decisions of public and/or private sector.

- **Liberalisation**
  Freely allowing or easing the entry and exist for the competitors in the market.

- **Disinvestment**
  Sale of government shares or assets to the private sector.

- **Restructuring or reforming public sector**
  By retaining ownership with the government, changes in the performance is brought through organisational restructuring or changes in the style of management or functioning.

- **Competitive Tendering or Contracting Out**
  Introduction of competition from private sector for public services provision traditionally supplied in house by direct labour. For eg. The collection and disposal of domestic refuse. Contract will go to the lowest bidder to provide quality of output.

- **Public Floatation:**
  Shares are offered to the general public and can be traded subsequently on the stock exchange.

- **Placing:**
  Brokers acting on behalf of a government arrange for the purchase of shares by placing them with a group of investors or large investor who may wish to hold or sell off the stock.
• **Trade Sale**
  A State enterprise sold to a private sector company or consortium. A trade sale is likely to be on the basis of a tender and financial markets are bypassed.

• **Management/Workers buyout**
  A state owned undertaking is brought out by management and/or workers

• **Auction**
  Sale of the properties of the state owned undertaking is auctioned to the highest bidder.

• **Grant of Statutory right to purchase**
  Government grants statutory rights for the people to purchase specified state property after meeting certain specified requirements.

• **Voucher system**
  In which vouchers are handed over by the Government to the employees for investment in the privatised public sector undertakings either directly or through holding companies.

• **Franchising**
  Selling the right to supply a regulated market whose product generates revenue. For example, the provision of scheduled rail passenger services on the separately owned rail track network. The contract will generally go to the highest bidder and/or the bidder who promises the best quality of service.

• **Golden Share**
  This is a special share held by the Government in the privatised company to ensure that the activities and ownership of a privatised entity did not conflict with the national interest of the company. This would also help in ensuring that public interest is not undermined or diluted by any resolution of the Board of Directors of the privatised company.