CHAPTER II
PUBLIC SECTOR ENTERPRISES AND ITS
FINANCIAL MANAGEMENT – AN OVERVIEW

Section one of the present chapter deals with an Overview of Public Sector Enterprises in the world, India and Kerala and Section two deals with the Financial Management practices of Public Sector Enterprises in Kerala.

Section 1: Public Sector Enterprises – An Overview

Since the time of the great depression no one is left with any doubt that “the invisible hand” does not work the way it was contemplated, even if the individual initiative is allowed the maximum possible free play. The theory that if the government is kept out of the business, it would automatically provide the community with all it desired, without any plan or conscious planning opened the door to the devil has long ago been exploded.

Government intervention in the economic system for social and economic reasons is now clearly accepted and has come to stay. Governments all over the world, particularly in developing countries, have gone far beyond the indicative planning to price, wage, and numerous other controls and to state entrepreneurship.

Radical transformation from a purely agrarian economy to one of the important industrialized nations of the world, and demolishing of a regimented structured society to one based on social justice, would not have been possible without the emphasis which has been laid on the growth and development of Public Enterprises.
Even in developed countries, when other avenues fail, the State alone comes to the rescue. Most railway systems in the world have an extensive history of government initiative and subsidy. For supersonic travel or communication by way of earth satellites, state initiative is accepted without hesitation. Similarly, for the development of atomic energy there was no alternative to government action. These were big leaps from many developed counties, where the market could not be relied upon. For a developing country, a steel mill, a heavy engineering industry, a machine tool plant or production of basic chemicals or intermediates are its big leaps, which require a comparable initiative by the state.

It is important to remember, that much of the losses and shortcomings of Public Enterprises are really overheads of national economic development which get reflected in the books of many Public Enterprises. It is worth considering whether the cost of “national gestation” be treated differently instead of being debited to Public Enterprises. In countries where private enterprise heralded industrial development, these costs where borne:

i. Through bankruptcies of some enterprises

ii. By virtual enjoyment of monopoly power over a span of time sufficient to compensate high initial costs and losses

iii. Subsidies offered by the government (as in railways); and

iv. Through multi national operations with all its consequences
Meaning of Public Enterprises

Meaning of the term “public enterprise” continues to remain vague and varying. It is rightly said that Public Enterprises “is a neat label for a very untidy concept"4. Public Enterprises is a general word which masks very different realities. There is no authoritative internationally accepted definition of the term Public enterprise. It is each country’s prerogative to draw the line between public enterprise and other government organizations and activities. The line may not always be logical or rational. For example, in India a large number of departmental ordinance factories5 are not considered Public enterprises, but the Bharat Dynamics Ltd, which supplies defence equipment like other ordinance factories, is treated as a Public Enterprises because of its legal autonomy.

The word “public” has varying connotations6. It is used in the context of accessibility and benefit to the general public as in the terms “Public Services”, “Public Parks” or “Public Through Fare”. It is sometimes used to denote ownership by members of the public at large as in the term “Public Limited Companies”. A third sense in which it is used is ownership and control by public authorities in the interest of the public at large, and this is relevant here. The public purpose is the very core of Public enterprises. The very rationale of Public Enterprise is the desire to attain some broader developmental goals and a range of socio economic objectives. It is in this sense that Public Enterprises are often described as “instruments of national policy”. The public purpose or interest may be affected by interest groups having varying views on what constitutes public purpose or public interest, but it is finally determined by duly constituted public authorities, that is, the
government – central, state or local and changes in government could lead to a redefinition of what is public interest for a public enterprise.

The public ownership would cover central, state and local governments, as well as autonomous public institutions. The ownership is thus held directly or indirectly through the shareholding of public enterprises. The ownership should be more than 50 per cent to ensure managerial control. Even if the ownership is less than 50 per cent, the enterprise could acquire a public enterprises character, if the minority ownership is accompanied by an adequate measure of public control and public management. In many cases in India, the government has a substantial and even majority holding in major private sector companies via the public financial corporations, but as this is not accompanied by public management and public control these enterprises cannot be called public enterprises.

For companies under Section 619B of the Companies Act, 1956, 51 per cent or more of the paid up capital is held by the government along with one or more public enterprise, or by one or more public enterprise, without the government holding any direct interest. These enterprises have only partial public control because of the provisions of section 619 of the companies Act regarding the appointment of auditors by the government on the advice of the Comptroller and Auditor General (CAG).

Public control is another essential characteristic of public enterprise. This control is different from the regulatory, legislative and executive controls exercised over the entire economy by the government. It refers to the exercise of top management functions of Public Enterprises. The implications of public control are
public management, that is, top Public Enterprise managers are appointed by owner public authorities.

Regarding the “enterprise” aspect of public enterprise, they have a business character which is more likely to be found in areas of economic activity such as agriculture, mining, manufacture, utilities, construction, commerce, communication, finance and services. On the other hand, public administration, national defence, education and a variety of cultural and social services generally do not lend themselves to the business idea.

The business character implies capital investment in which the investors would normally expect a return. For this purpose, the goods and services could be made available by a Public Enterprise for a price, which may be adjusted from time to time to cover the cost of inputs. Public enterprise is assumed to be an institution with a business character, which would market its available output either to the government or to the public at large and charge a price for it.

Public Enterprises are transformers of our economy. Their contributions are manifold: investment in infrastructure, securing balanced regional development, creating new skills and competence, generating new employment potential, meeting many social obligations including preferential employment of certain backward and deprived communities, developing backward regions, securing economic self sufficiency through import substitution, projecting themselves as model employers and utilising the goodwill of other for the country’s development.
**Definition of Public Enterprises**

Public Enterprise is an organisation which is owned by public authorities, to the extent of 50 per cent or more, is under the top management control of the owning public authority, is engaged in activities of a business character (involving the basic idea of investment and returns), and it markets its output in the shape of goods and services for a price.

The Five Year Plan and other official documents also use the term “Public Sector” in the wider sense to cover all governmental activities, including public industrial and commercial enterprises.

Another term used for Public Enterprise is “Public Undertakings”. Strictly speaking, any activity of the government –business or otherwise—is its undertaking, but the term perhaps has limited use for industrial and commercial activities. It is used with reference to the parliamentary committee on “Public Undertakings”. But the very same enterprises as covered by the parliamentary committee are dealt with by the “Bureau of Public Enterprises” in the Ministry of Industry.

Public Enterprises are also referred as “Government Controlled Enterprises”, “State Economic Enterprise”, and “National Companies “. In U.K. Public Enterprise is known as “nationalized industry’ because most of the Public Enterprises there were the result of nationalization of existing industries. A British author opposing the use of the term “ nationalized industry” said that he preferred to call them “national business” to avoid nationalized , which seems to give a permanent emphasis simply to a process of public acquisition.
In many Latin American and African countries, Public Enterprises is known as “parastatal” or “parastatal sector” that is, the group of institutions, organisms and enterprises that, empowered by the State, cooperate in its aims without being part of the public administration.

**A Rationale For Public Enterprises**

Public enterprises occupy a vital role in the economy of almost all countries of the globe irrespective of their political affiliation. Still, if one analyse the ultimate causes of the emergence of public enterprises, it varies from one country to another. In the western countries, the reason could be located with infeasibility of application of laissez faire policy and widespread social tensions created by capitalism that resulted in the emergence of public enterprises. The classical economic view of laissez faire aimed at full employment, full investment and maximum wealth. However, in actual practice, underemployment, exploitation, inequality in the wealth distribution and poverty were the after effects.

The important reason for the origin of public enterprises was that through private capitalism, the total society was divided into two classes, namely, ‘the haves’ and ‘the have-nots’. The introduction of private capitalism has totally neglected the economic health, security and welfare of the masses. Only through state participation in industrialisation, equitable distribution of wealth can take place. To ensure the health, security and welfare of the citizens, initiation of state enterprises is the only answer. Another important reason in favour of public enterprises is that private capitalists will never invest money or undertake those ventures which have a long gestation period. They will hesitate to start such ventures, because their capital
will be blocked up in those projects for substantially longer duration. In this situation too, public enterprises provide the only solution. Public enterprises give more importance to economic and social welfare and they are not bothered about long gestation periods.

Another argument put forward by the authorities for public enterprises is that they are able to satisfy a number of social obligations at a time. They have to start industries in those areas which are not commercially feasible. Simply because of this reason, these public enterprises have to sell their customers’ goods at prices lower than their costs. Some may point out that the performance of public enterprises is to be evaluated not on a financial basis, but on the basis of social service indicators, like total amount of production, total number of employment opportunities created, total contribution made by public enterprises to the government exchequer in the form of taxes and interest. In their opinion, financial yardsticks should not be used for evaluation of performance of public enterprises.

According to Jain (1967)⁹, in the modern world, the laissez faire policy has no existence. It is absolutely improbable and impracticable to think about non-interference of government in business matters. Proper intervention of Government at the right time in the industrial matters of a nation will provide for its economic development. The affairs of government industry and trade have got so much mixed up that their separation is neither easy nor desirable. As rightly pointed by Aravind Gupta (1984)¹⁰, when we summarise the causes of the emergence of public enterprises, globally, it is found that there are two major compelling factors for the government to participate, first, the risk involved in the enormous capital investment
in certain key industries and secondly, the need to achieve and maintain certain desirable socio-economic objectives.

**Public Sector Undertakings – The Global Scenario**

Once we compare the growth of public enterprises in the capitalist and socialist countries, we can find that the capitalist countries started public enterprises in order to reconstruct their economies after World War I, or to accelerate the pace of their development or to save their economies from the ravages of great depression. Singh (1986) further clarified that in the Communist countries, public enterprises were formed as part of their ideological commitment.

Post-Second World War era is characterized by the emergence of large number of countries free from European Colonialism in Asia, Africa and North America. The options available with these countries were to accept the Capitalist System or Communism or to adopt a middle way encompassing the merits of both, the Mixed Economy. It has been proved beyond doubt that both developed and developing countries have used Public Sector Enterprises as a vehicle for their sustained development. For instance, in the United States of America, where private sector enterprises are playing a vital role in the economy, critical areas of essential services are managed by Public Sector Enterprises.

To quote Juma Walter Mwapachu (1983), “in a capitalist market economy as that of the United States of America where the private sector constitutes the core of economy, we find perhaps the most well managed public enterprises covering critical areas of essential services like energy, water transport, postal services, airlines and defence production”. As is observed by Khera (1977), the whole of
Coal industry in Britain is nationalized. Other Government enterprises in Britain include activities so diverse as the production and distribution of electricity and gas and the operations of airlines and road transport. Likewise, Italy which is the member of the Western European Common Market has a nationalized oil industry. Besides this, the Government owns and manages a large number of industrial and commercial undertakings, such as railways, steel plants, mines, chemical factories, engineering establishments and banks.

According to Singh (1986)\textsuperscript{14}, in France, even towards the end of the second world war, the policy of nationalization had been vigorously pursued in coal, mining, gas and electricity industries. The Bank of France and several other big banks and insurance companies were nationalized. Khera (1977)\textsuperscript{15} went on to tell that the story of Canada is also not different. In Canada, public corporations have existed over a century. But it was in 1940, that they were given legislative recognition. These corporations cover a wide field of activities such as the operation of railways, steam ships, air services and harbour facilities, operation of arsenals, atomic energy, television and radio. In Mexico, oil production and prospecting is done by nationalized industries. The Petroleos Mexicans, a nationalized industrial undertaking in Mexico has a monopoly over oil prospecting and production in the country.

Thus it is evident that public enterprises were organized in both capitalist and socialist countries. Socialist countries across the globe were not exceptions as far as the theory in support of public enterprises is concerned. As is opined by Mishra and Shankar (1986)\textsuperscript{16} in socialist countries, the organization of public enterprises was a matter of policy, to check monopoly and to avoid concentration of economic power.
in the hands of private individuals. In USSR (now Commonwealth of Independent States) after the October Revolution of 1917, the Bolshevik Party took over the state power and proclaimed that its first objective was the creation of society and in the distant future a communist party. As pointed by Das (1966)\textsuperscript{17}, the roots of exploitation have been seen in the institution of private property. So private property has to be abolished in a series of steps and the public sector has to be the engine of development. The Constitution of USSR laid down that the economic foundation of the nation is the socialist system of economy and the socialist ownership of the instrument and means of production and the elimination of exploitation of man by management. In his study Nataraja Iyer (1995)\textsuperscript{18} made a reference about China’s initiative towards this. Though China initially started with a slight tilt towards private participation slowly it could scan the environment and the Chinese constitution granted equal opportunity for the development of public and private sector undertakings. Later, this policy was changed and the entire system was brought under the control of the State.

In the developing countries, there is lack of private capital, absence of technical know-how and want of managerial expertise. In these circumstances, as explained by Nataraja Iyer (1995)\textsuperscript{19} only through the development of public enterprises can these countries plan their economic development. So they invest huge sums of money in the public sector. As opined by Aravind Gupta (1984)\textsuperscript{20}, in developing countries, public enterprises are viewed as an effective instrument to break the longstanding stagnation and thereby facilitate economic development. With this conviction most of the developing countries have invested massive resources for the promotion of public enterprises.
**Evolution of Public Sector Enterprises in India**

In India, modern industries emerged during the pre-independence period itself. Post partition, India got 77 per cent of the total area of the undivided country with 82 per cent of the total population, 91 per cent of the total number of industrial establishments, and 93 per cent of the total number of workers employed (Kuchal 1989). We have identified the importance of self reliance and decided the pattern of investment in the industrial sector by giving top priority to build adequate capacity in basic industries such as steel, non-ferrous metals, capital goods, fertilisers and petro-chemicals. The public sector was given the task to assume a major role in the expansion of these industries which they have fulfilled to a great extent with plan support.

In the public sector, problems began with cost and time overruns in a large number of projects. Post commissioning, inefficiency tended to persist at the operational stages of the projects. The widening technological gap between the Indian industry and the rest of the world also had contributed for obsolescence, raising costs and poor quality compliances. As capacities remained underutilized in many industries, the shortages in production, apart from eroding the economic viability of the units, had a chain reaction within the industrial sector, more specifically in public sector. Hence, it is a well thought and conceived idea to bring into picture a mechanism that not only provides a sound platform to rebuild the industrial units in deep trouble but also to pull back potential sick units from imminent disaster. As a bail out option evolved was the BIFR, which came into existence with the passing of the Sick Industries Companies (Special Provisions) Act, 1985.
India was one of the major nations who opted for a mixed economy. Resultantly, the public undertakings have come to play an important role in India. The distinction between private sector and public sector in India became clearly pronounced only in the post independence era. Of late, the Government has accepted the concept of welfare state and socialistic pattern of society as its ultimate aim. The mixed economy concept envisaged by the Government of India implied the creation of two definite and well defined segments of the economy, viz., public and private. Of these the public sector is called upon to play an increasingly predominant role in the planned economic development of our country. They help to promote self-dependence in strategic sectors of economy, build up a balanced infrastructure for the development of a nation to accelerate industrial development and encourage social control on trade and industry for ensuring equitable distribution of goods and services. Public enterprises, in addition to the above achievements, create more employment opportunities, reduce disparities in income and wealth, and also check the growth of private monopolies.

Prior to 1947, there was virtually no public sector, barring the field of transport and communication, Railways, Postal and Telegraph, etc. have been managed by the Central Government since pre-independence period. During the post independence period, the growth and development of industries in India has been largely governed by the Industrial Policy announced by the Government, in 1948, which placed the responsibility for the economic welfare of the people on the State. In pursuance of this policy, government decided to enter the field of industry and defined the scope of activities for the public and private sectors. The Industrial Policy Statement, 1948 needed to be modified to suit new challenges and changing
conditions. As a result Government of India issued Industrial Policy statements in 1956, 1973, 1977, 1980 and 1991. In each of these documents, the role of the PSUs in India in the process of industrialization has been clearly spelt out.

The Industrial Policy Resolution 1956 stated that in order to realise the objectives of the socialistic pattern of society, it was essential to expand this sector. This would provide the economic foundation for increasing opportunities for gainful employment and improving living standards and working conditions for the mass of the people. It would also reduce disparities in income and wealth, present private monopoly and the concentration of economic power in the hands of a small number of individuals. The adoption of the socialistic pattern of society as the national objective, as well as the need for planned and rapid development requires that all industries of basic and strategic importance or in the nature of public utility services should be in the public sector. Other industries which are essential and require investment on a scale which only the state, in present circumstances could provide have also to be in the public sector. Accordingly, the state must progressively assume a predominant and direct responsibility for setting up new industrial undertakings and for developing transport facilities.

Though the State enterprises have now become a world wide phenomenon, in the Indian perspective, it bears more weight probably because of our new experiment of mixed economy. Since, its existence, the public sector in India has made a tremendous rise. With a vital role thus assigned to the public sector it is important that public sector enterprises should flourish and make their due contribution towards the economic progress of the country. It has made a valuable contribution
to the industrial modernization of the country, building up vitally important infrastructure for economic growth and in achieving a degree of import substitution.

When India became independent, it had a population of 370 million mostly illiterate. Its agriculture and industrial sectors were in primary stages of development and the per capita income was estimated at Rs. 200. At this stage it is the public enterprises which had to lay the basis upon which the structure of a dynamic and diversified economy is to be built up. Before the initiation of planning in India, public sector used to restrict its activity to sectors like railways, ports, communication, broadcasting, irrigation, power and a few departmental industrial undertakings. After the commencement of five year plans and the declaration of industrial policy resolutions, public sector started to cover a vast and varied range of activities. It occupied a dominant position in the basic industries and capital goods industries. It could provide the required impetus in the development of backward regions also. It is expected that the public sector will give relief to the economic strain that is being experienced by our country.

**Role of Public Section Enterprises in Industrializing India**

As highlighted by Sharma (1975)\(^2\), contributing an estimated 11.12 per cent of Gross Domestic Product at market prices in 2005-06, the Central Public Sector Enterprises (CPSEs) continued to be engaged in the production and supply of a wide range of products and services including basic goods like steel cement and chemicals, capital goods like pressure vessels, boilers and drilling rigs and intermediate goods like electricity and gas. They also rendered a large number of services like telecommunications, tourism and warehousing.
The role played by the CPSEs in industrialization of Indian economy can be visualized from the following facts as sourced from the Review of Central Public Enterprises\textsuperscript{23} by the Bureau of Public Enterprises (Govt. of India, 2008):

1. Cumulative investment of all CPSEs as on 31\textsuperscript{st} March 2007 amounted to Rs.3,93,057 crores. The share of manufacturing enterprises in such investment was the highest at 51 per cent followed by service sector enterprises at 40 per cent and mining at 7 per cent.

2. In terms of capacity utilization, 51 per cent of all Central Public Sector Enterprises operated at 75 per cent or higher; 16 per cent at 50-75 per cent and the residual 33 per cent at less than 50 per cent.

3. The long term loans of CPSEs went up to Rs. 3,61,714 crores.

4. The accumulated losses of all CPSEs declined by Rs. 10,578 crores from Rs. 83,725 crores in 2005-06 to Rs.73,147 crores

5. 44 CPSEs are listed on domestic stock exchanges while shares of MTNL (ADR) are listed on New York Stock Exchange, the shares of GAIL and SAIL are listed on London Stock Exchange.

6. In net value addition of CPSEs at market prices, the share of taxes and duties was the highest at 46 per cent, followed by net profit (26 per cent), salaries and wages (19 per cent) and interest (9 per cent).

7. At the end of March 2007, the 239 CPSEs employed over 16.49 lakh people excluding casual workers. The comparable figures in the previous 4 years were 19.92 lakh and 18.66 lakh, 17.62 lakh and 17 lakh respectively.
Even though the Indian PSUs show a rosy picture, some setbacks can also be seen among them. Hence, efforts are being made to modernize and restructure sick CPSEs and revive sick industry. Only the chronically loss making CPSEs are considered for closure or sell-off, after payment of due compensation to their laid off employees. The problem of sickness in CPSEs is addressed by the Administrative Ministries and Departments by evolving an appropriate need based strategy concerning a particular CPSE. Government further helped the CPSE to turn around financially, set up the Boards for Reconstruction of Public Sector Enterprises (BRPSE) in December 2004 to recommend measures for restructuring/reviving CPSEs referred to them. The BRPSE also recommends cases where disinvestments or closure or sale are justified. Till 31st October 2006, BRPSE has made recommendations in respect of 36 CPSEs and Government has approved the proposals in 21 cases (Bureau of Public Enterprises, 2008).

In order to ensure and encourage efficiency in their functioning, Government has taken various steps to professionalize the Boards of CPSEs. These include provision of outside professionals in the form of part-time non-official directors, restricting the number of Government nominated Directors to one-sixth of actual strength of the Board subject to a maximum of two, and incorporation of functional directors up to a limit of 50 per cent of actual strength of the Board (Bureau of Public Enterprises, 2008).

On the recommendations of Arjun Sen Gupta Committee, the Government during 1987-88 introduced the concept of Memorandum of Understanding (MOU) to ensure clarity in the functioning of CPSEs and proper balance between accountability and autonomy for better results. The number of CPSEs signing MOU
went up from 4 in 1987-88 to 112 in 2006-07. In order to further the competitive spirit, an attempt has also been made to evaluate the performance of the CPSE on the basis of (a) sales (b) growth of sales (c) net profit (d) growth in net profit (e) return on net worth (g) earning per share and (h) dividend pay out ratio (Bureau of Public Enterprises, 2008)26.

The Government policy on disinvestments has evolved over the last decade and is generally announced through the budget. Disinvestment of Government equity in CPSEs began in 1991-92. Till 1999-2000, disinvestment was primarily through sale of minority shares in small lots. Between 1999-2000 and 2003-04, the emphasis of disinvestments changed in favour of strategic sale. The proceeds from disinvestment from April 1991 to March 2007 amounted to Rs. 49,241.29 crores. At present, the policy is to list large, profitable CPSEs on domestic stock exchanges (Bureau of Public Enterprises, 2008)27.

Public Enterprises Policy

In any scheme of economic liberalization, a proper sequencing of reforms is very vital. It may be observed that to begin with reforms around the world were initiated with Public Enterprise restructuring. India did not pay any heed to this critical dimension of reform. Not to mention, the first generation economic reforms, there is no clarity about the approach to be adopted with regard to Public Enterprise restructuring as a part of second generation reforms. The reforms in their first stage have more or less been limited to the central government. Consequently, the talk about reforming the Public enterprise has veered around only the Central Public Enterprises leaving out of its scope a vast number of State Level Public Enterprises,
municipal enterprises and co-operatives with a majority shareholding of the government. Besides the impact of coalition politics, the lack of bureaucracy has been the principal cause of shying away from formulating a transparent Public Enterprise reform policy.

**Policy Measures in 1990s**

Between 1990 and 1999 there have been frequent changes in the government, barring July 1991 to June 1996 during which period a minority government was at the helm of affairs. The year 1990 saw two governments, both of which were the byproducts of coalition. During the year, the thought of employee stock ownership in public enterprises gained momentum and worker’s participation in management assumed ascendancy. The concept of regulated growth in investment in public enterprise marked its emergence.

**Between 1991 - 1996**

The fiscal crisis reached its peak in 1991 and the government had to approach global financial institutions for stabilisation and structural adjustment. As part of the conditionalities imposed, the government had to announce some important measures to restructure public enterprises.

**Portfolio**

It was decided to review the portfolio of public sector investments with a view to focus on strategic, hi-tech and essential infrastructure. Consequently, enterprises which were operating in competitive sectors of the economy where the private sector had registered its emphatic presence were decided to be hived-off.
This policy pronouncement provided a forceful hint to public enterprises to review their spectrum of activities with the objective of unloading non core and peripheral functions. It was expected that the follow up of this measure would result in making public enterprises lean and mean. The government felt that a selective public enterprise portfolio would bring down the transaction cost, improve the quality of control and add to the efficiency of the public enterprise system.

**Reference to Board for Industrial and Financial Reconstruction (BIFR)**

At the beginning of the 1990s itself, a large number of public enterprises had fallen sick. They constituted about 25 per cent of the then operating public enterprises. The trends in the financial results of the remaining public enterprises revealed the likelihood of more public enterprises falling sick. The government did not have an exit policy for public enterprises and it refrained from following the path adopted by the private sector. It therefore, decided to use the BIFR route, which provided a fair opportunity to public enterprises to evolve suitable revival packages and implement them or else wind up with a social safety net. Unlike the private sector which throws away the baby with the bathwater, the government suggested public enterprises to have a human face. Each enterprise was directed to formulate its own social safety net comprising voluntary retirement, and retaining and redeployment schemes for workers. The government made an announcement to set up the National Renewal Fund (NRF), the finances for which had to be gathered from global agencies, while parts of the proceeds were to come from disinvestments.
Mobilisation of Funds, Disinvestments and Public Participation

The 1990s started with a severe resource crunch. In February 1990 the coffers of the government did not have adequate money to pay for the employees’ salaries. This was an adequate hint about the shape of things to come. The constant increase in social sector spending and the move to curtail fiscal deficits did not leave much scope for public enterprise to depend on the government for funding. The government permitted public enterprises to access international capital markets and make forays into the Indian capital market. The partial disinvestment in public enterprises was introduced as a double edged sword aimed to reduce, on the one hand, the fiscal deficits of the government, and enhance the degree of publicness in public enterprises, on the other, through wider participation in their shareholdings by general investing public, banks, mutual funds, workers and financial institutions.

Upgradation of Technology

For the introduction of the state of the art technology, it was decided that public enterprises would be given a free hand and the funds for such upgradation would come from the disinvestment proceeds or restructuring packages approved by the global financial institution.

Governing Boards

It was realised that strengthening the institution of the Governing Boards was necessary in order to professionalise public enterprises and make them effective business entities. A number of steps were suggested for revamp. It was decided that the number of government nominees was not to exceed two. Further, part time directors were expected to bring in a breath of fresh air to the public enterprises and
were to have a greater say. More room was made for the representation of professionals, who were expected to provide sound business advice. The representation of different interest groups also received attention and the worker’s representation on the Boards was accepted in principle.

**Accountability and Autonomy**

To solve this tangle, the government emphasised the need for widening and deepening the concept of Memorandum of Understanding. It wanted the contracts to be negotiated well in advance and subsequent delegation and decentralization of powers within the enterprise. It advocated sincere involvement of public enterprises in the formulation and implementation of Memorandum of Understanding to thwart unnecessary public criticism on the count of public accountability, conferment of greater autonomy to these enterprises gradually over a period of time with regard to matters concerning capital expenditure, mobilisation of funds, formulation of incentive schemes and joint ventures.

**1997 Periods**

The Janata Dal Government, during this period, initiated some important measures and made public its unambiguous stand of speeding up the disinvestment process through majority stake in shareholdings.

**Disinvestment Commission**

The government set up through an executive order, the Disinvestment Commission which was responsible for reporting its scheme on the disinvestment of
selected public enterprises. It was also empowered, among other things, to suggest to the government the appointment of global advisors.

**Navratnas and Miniratnas**

In order to prepare giant public enterprises for global competition and enable them to assume the role of India multinationals, the government identified 9 enterprises namely, 1. Bharat Heavy Electricals Ltd, 2. Steel Authority of India Ltd, 3. Oil and Natural Gas Corporation, 4. Videsh Sanchar Nigam Ltd, 5. National Thermal Power Corporation, 6. Bharat Petroleum Corporation, 7. Hindustan Petroleum Corporation Ltd, 8. Indian Oil Corporation Ltd, 9. Indian Petrochemicals Corporation Ltd, as navaratnas and 97 enterprises as miniratnas based on their record with regard to constant profitability and size of capital. Later, the list of navaratnas was extended from 9 to 11. Subsequently, the number of miniratnas was scaled down from 97 to 45. The rationale behind identification of these enterprises as navaratnas and miniratnas was to increase their economic and operational autonomy in proportion to their financial and commercial success, as also to provide them special leverage to face competition in Indian and global markets by freeing them from bureaucratic and procedural hurdles.

**1998 periods**

The coalition government during this year had to do a lot of tight rope walking with the left front and had to therefore adopt a mild posture with regard to off-loading public enterprises from its portfolio.
Rehabilitation Package

The government decided to prepare rehabilitation packages for sick public enterprises to give them a chance for revival instead of going for their quiet closure/privatisation.

Refining the scope of the Disinvestment Commission

The government wanted the commission to make suggestions regarding disinvestments of only those enterprises which it referred to the commission. The commission was divested of its powers to recommend the names of global advisors.

1999 Periods

The rightist government of the day was prepared to accelerate the tempo of the disinvestment programme and reduce the scope of public enterprise activities in the Indian economy.

Privatisation

For the first time, during the 1990s, the Government in its budget presented to the Parliament used the word privatisation. The Government went all out to show its commitment to privatize public enterprises and restore the powers of the Disinvestment commission.

Competition

The government initiated the process of evolving a competition policy. It exhorted public enterprises to be competitive.
Salaries and Wages

While accepting the Mohan Committee report on wage revision in public enterprises, the government left it to each and every public enterprise to examine its paying capacity to meet the burden arising out of its implementation. The government categorised public enterprises into 3 divisions:

Public enterprises earning profits continuously for three years; public enterprises recording mixed performance; and public enterprises suffering from sickness. Those enterprises which were consistently earning profits could implement the revision, the mixed performance enterprises were required to take the approval of the respective ministries and the sick enterprises had to get the burden of implementation incorporated in the rehabilitation packages.


The government decided to discontinue the National Renewal Fund in its present form and place the funds required for retraining/rehabilitation of employees who had availed VRS under the Department of Public Enterprises. The Department of Public Enterprises involved itself in this work from 2001-2002 with a plan fund of Rs 11.50 crores. The Department of Public Enterprises were concerned with the employees of the Central Public enterprises. The Ministry of Labour and the Ministry of small scale industries were concerned themselves with the employees of the State Level Public Enterprises.

The period 1991-92 to 2001-02 saw a series of policy measures aimed to dismantle public sector to give fillip to private monopoly and increase the dependence of the Indian economy on global economic powers.
History of Industrialization in Kerala

A study of the public sector in the State of Kerala will naturally have to be in the context of the philosophy of Government of India so far as public undertakings are concerned. However, it has to be emphasized that the public sector in Kerala has a much longer history than that of India in general.

As is observed by Velu Pillai (1940)\textsuperscript{28}, under the close supervision of the Maharaja Marthanda Varma (1729 AD to 1758 AD) a commercial department was organized. The Government possessed monopoly over many articles of trade. Depots were established in different places. In them were stored pepper, tobacco, areca and other articles which were purchased at rates fixed by the Sircar (Government) in pursuance of a royal proclamation. The State initiative on this account has commenced of its own. Sukumaran Nayar and Gangadharan Pillai (1980)\textsuperscript{29} had opined that industrial development under the State auspices in the Princely State of Travancore and Cochin was not part of an all India effort at planned economic development. A number of Public Undertakings like the State Transport Department (later on converted into the Kerala State Road Transport Corporation - KSRTC), the State Electricity Department (later on converted into Kerala State Electricity Board - KSEB), the Trivandrum Rubber Works, Government Ceramic Concern, Kundara, the Travancore Plywood Industries and the Fertilisers and Chemicals Travancore Ltd, Alwaye were started during the period of Princely Rule in the State of Travancore. In Cochin State, the Government Pottery was started.
The absence of a national policy was felt during those days itself. According to Sreedhara Menon (1965), the policy of building up of public sector in the Princely States of Kerala before independence involved a number of issues. First, there was no attempt to chalk out a comprehensive industrial plan. Secondly, the emphasis was on starting a few industries. Thirdly, the importance of industrial development was dependent on the personality of a few Devans like M.E. Watts, Sir C.P. Ramaswamy Iyer and R.K. Shanmughom Shetty (the First Finance Minister of Independent India). Fourthly, there was no link with an All India Scheme of development. The assumption was that the Princely States would remain autonomous and self-sufficient without being part of an All India Federal Union.

The Industrial Policy Statement (1960) of the Congress Praja Socialist Party Coalition Government led by Mr. Pattom Thanu Pillai stated that the State would give maximum aid to industrialists coupled with a fair deal to labourers. This created confidence among private entrepreneurs. In short, the climate was more favourable and the State was proceeding steadily towards the goal of industrialization. The main programmes under large and medium industries in the public sector during the period were related to the establishment of a few industries and the expansion and modernization of source of the existing industries.

The Kerala State Industrial Development Corporation Ltd. (1961), the Trivandrum Spinning Mills Ltd. (1962) and the Plantation Corporation Ltd. (1962) were established and the expansion and modernization of Rubber Factories at Trivandrum, the Kerala Government Ceramics, Kundara and the Oil Factory Division of Kerala Soaps and Oils, Ltd. Calicut was also undertaken. The Marxist led United Front Government in its Industrial Policy Statement in 1967 stated that
the state would function within the limits of the policy laid down by the Government of India. The Statement said that the Government’s policy would be directed not to thwart or impede any effort, but to smoothen the process. The Government indirectly conceded in the industrial policy statement that the performance of the Public Sector Undertakings in the State was unsatisfactory. The Government’s determination to do away with this unhealthy condition was also embodied in the policy statement.

**Drawbacks of Industrialisation in Kerala**

Many criticisms have been levelled against the unhealthy operation of the Undertakings like the KSRTC, KSEB and many units like the Trivandrum Rubber Works Ltd., the Kerala Soaps and Oils Ltd. and The Kerala Ceramics Ltd. According to Gangadharan Pillai (1980)\(^{32}\), the public enterprises occupy a crucially important position in the economic set up of the State. They provide the industrial infrastructure in the State and also accelerate the rapid economic development. But unfortunately, most of these undertakings in Kerala have been haunted by one problem or the other which have defied easy solution. Quite surprisingly, no attempt has been made so far as to analyse the various aspects of the administrative problems of the State undertakings.

The Committee on Public Undertakings of the LokSabha in their Report on Planning, Management and Administration of Kerala State Government Companies (1966)\(^{33}\), has observed inter alia that Board of Directors should, apart from its role of advising and guiding the affairs of the Company, be able to initiate, decide and supervise. To that extent it is not enough that the Directors merely safeguard
Government’s interests in the organisations but they should be able to play a more positive role in conducting the affairs of the Undertakings by fully appreciating its commercial character and adopting policies.

Inadequate capital is another problem facing these enterprises. The Government is unable to provide adequate finance due to its financial stringency. The public enterprises on their part are also unable to generate reinvestible capital. No public enterprises can achieve its objectives unless it gets sufficient capital to undertake its various activities as opined by Gangadharan Pillai (1980)\textsuperscript{34}. The third problem which plagues these enterprises is the unscientific method of recruitment of personnel. Persons are recruited to these business concerns as if they are recruited to a regular Government Department. Naturally, this affects the operational efficiency of the concerns.

As far as Kerala is concerned there is acute unemployment among the educated. Government is the biggest employer and it often comes under heavy pressure to provide employment to the educated young men and women. The way in which the Government makes appointment is zealously watched over as there is tough competition among the candidates. Therefore to avoid criticism the Government handed over the responsibility of recruitment to the public service commission. The Public Service Commission is governed by the rules regarding reservation of a particular quantum of posts of certain castes and communities. The net result is that public enterprises were often viewed as arms of the parent Ministries, instead of treating them as autonomous commercial institutions to be operated by trained personnel selected on the basis of merit irrespective of caste or community. There is wide difference between departmental functions and activities
of manufacturing units. The success of Public Enterprises depends on the efficiency of each individual, right from the watchman to the chairman. The absence of competent persons to manage enterprises is likely to create a lot of problems of production. Such situations have also arisen in some of the state enterprises in Kerala.

Political interference or ministerial interference is another major curse on the public enterprises. Every Ministry wants to retain tight control over these concerns and no concern was ever permitted to function as an autonomous body. Intense political interference is often felt in the matters of appointment of Directors and other top officials as well as formulation of policies in these concerns. This does not however mean that the Boards of Public Enterprises should be independent. So long as the concerned Minister has powers to give general directions, there is no limit to the authority which he can wield. Hanson (1962)\textsuperscript{35} has approvingly quoted Paul. H. Appleby to say that true autonomy is out of the question and not even seriously proposed by any informed men. In a democratic set up, Government can always and should always, be in a position to intervene in any matter, really important to the development of the industry. The decisive moment of ministerial intervention, is when the top level managerial appointments are being made. Government also has the very important duty of providing the kind of basic organization framework which will facilitate good management. It does not matter very much whether that framework is called a Government Department, a Public Corporation or a State Owned Company. The vital thing is that it should be well designed. It should then leave the management to get on with the job with the minimum interference, ie.
interference only at certain strategic points. Then at intervals, it should check their performance.

As regards the size and composition of the Board of Management in Public Enterprises in Kerala, there are no recognizable rules as revealed by the study conducted by Gangadharan Pillai (1980)\(^\text{36}\). The maximum number of the Board of Directors is specified in some case, but the minimum number is specified in all cases. Similarly, the qualification and experiences of some members are specified but are silent about other, thus providing necessary flexibility for making the choice of members from any sources the ruling party or Minister may deem fit. The tenure of the Board is specified in the case of statutory corporations, but the State Government is free to appoint the Boards for shorter periods. Though the Boards are considered to be autonomous bodies they virtually enjoy limited autonomy only. The Boards are given freedom for the day-to-day conduct of business, but policy matters such as enhancement of fare in the KSRTC, tariff fixation in the case of KSEB are decided by Government.

Another major problem experienced by state enterprises before the proclamation of National Emergency in June 1975 was gross indiscipline of the labour. The trade union movement is very strong in Kerala. As there are numerous parties and each party wants to have a labour wing there are several trade unions in one undertaking. As there is rivalry among them, workers were often persuaded to resort to strike work even on flimsy grounds. With the connivance of the politicians the public undertakings were used by the workers to extract maximum benefit for themselves and to do as little work as possible. Several cases were noted where workers got what they demanded. Bonus at the rate of 25 per cent was paid at a time
when the industry was actually incurring heavy losses. Incentive bonus was given when there was no production at all. The fact was that trade unions have been taken to the other extreme when workers, supported by the political leaders were dictating terms of the managements. In several instances there was actually the tyranny of the organized workers. There was practically no attempt made from any responsible quarters to set the matters right except during the emergency. Kerala among Indian States has a proud record of a steady growth of public enterprises.

The Government of Kerala constituted the Enterprises Reforms Committee (ERC) during November 2001 to recommend restructuring/reform options for the ailing public enterprises in the State. Since June 2002, the ERC has recommended reform measures in 45 State Level Public Enterprises and the Government has taken decision of 30 of these enterprises. About 4832 employees have been paid retirement compensation under the social safety net programme that consists of a financial compensation package and a welfare and economic sustainability package. Capacity building for reform implementation and post reform governance and development and performance monitoring of State Level Public Enterprises is undertaken by the Public Sector Restructuring and Internal Audit Board (RIAB), which is the Secretariat of the ERC. As at the end 31st March, 2008, there were 104 State Level Public Undertakings functioning in the State of Kerala. This include 17 units under Development and Infrastructure, 11 under Chemical sector, 14 under Plantation and Agro Based segment, 11 under Engineering, 9 Under Electronics, 4 Textile units, 7 Traditional Units, 5 Electrical Equipment manufacturing and remaining under sectors like, Ceramics, trading and wood based industries. The State Level Public Enterprises are under the administrative control of different
government departments. Fifty seven enterprises are under the Industries Department followed by 14 under the Agriculture Department.

**Budgetary Assistance**

The Budgetary assistance to State Level Public Enterprises has come down drastically as is finding it difficult to source the allocation from its revenue collections. It can be seen that the budgetary support is a paltry 0.60 per cent of the total budget outlay and out of the total support to all sectors 20.54 per cent is for Enterprises under Industries Department during 2006-07. In the year 2005-06 out of a total budget outlay of the State amounting to Rs.5369 crores, Rs. 50 crores was provided to the PSUs. Even though the total budget outlay of the State has increased to Rs. 6690 crores, assistance to the PSUs came down to Rs. 40 crores during 2006-07. This shows how fast the Governments are running away from the burden of providing the required financial assistance to PSUs which warrants the entities to make reasonable surpluses to plough back into their respective businesses.

**Section 2: Financial Management Practices of Public Sector Enterprises in Kerala**

The total paid up capital of the State Level Public Enterprises at the end of the year 2006-07 amounts to Rs. 5924.19 crores and the capital invested totalled to Rs.17852.80 crores. The turnover from sales during the year was Rs. 10,885.37 crores with a total profit standing at Rs.456.06 crores. While 50 enterprises have earned profits worth Rs. 816.13 crores, 64 Enterprises have reported losses amounting to Rs. 360.05 crores. The net worth taken together for the State Level Public Enterprises was Rs. 1518.92 crores after setting off the accumulated losses as
on March 2007 amounting to Rs.5815.14 crores. This means that the hard earned capital contribution of the State has eroded by more than 98 per cent by this time. The payment to the State exchequer by way of taxes amounts to Rs. 1800.83 crores (about 13 per cent of State Tax revenue), while the guarantee commission paid during the year was Rs. 19.36 crores. Amidst the loss making undertakings there were rays of hopes also and dividends worth Rs.13.27 crores have been declared and paid for the year by the profit making units 39.

Sources and Applications of Funds

It is observed that the State PSUs are excessively depending on external debt, both long term and short term versions in the absence of sufficient plough backs on account of internal accumulations. As on 31st March 2007, against a total share capital investment of Rs. 5924 crores by the State and the amount ploughed back by the profit making entities amounting to Rs. 3100 crores, the long term external borrowing stood at Rs.11929 crores and the same for shorter term at Rs.11612 crores. Out of this an alarming Rs. 7505 crores was utilized to fund the accumulated losses of loss making undertakings. A net fixed asset to current assets scenario is also not promising. Against a total of net fixed assets amounting to Rs. 10745 crores the investment in current assets stood at Rs. 13592 crores, which is putting pressure on the fixed assets (revenue generating) to generate additional returns to support the current assets (revenue maintaining assets) 40.

Investments

The total investment (capital invested) in public enterprises in the State as on March 31, 2007 amounts to Rs. 17852.80 crores. The investment was Rs. 18701.07
crores at the end of the previous year. The maximum investment is in Kerala Water Authority (Rs. 4701.97 crores). The other enterprises with major investment (above Rs. 500 crores) include Kerala State Electricity Board, Kerala State Housing Board, The State Power and Infrastructure Finance Corporation Ltd., The Kerala State Civil Supplies Corporation Limited, Kerala Financial Corporation and Kerala State Road Transport Corporation.

**Turnover**

During the year, the State Level Public Enterprises have together earned a turnover of Rs. 10885.87 crores during 2006-07 as compared to Rs. 9282.95 crores during 2005-06 (an increase of 17.27 per cent). The highest turnover has been achieved by Kerala State Electricity Board (Rs.4286.13 crores) followed by Kerala State Beverages (M&M) Corporation Ltd. (Rs. 1679.62 crores) and Kerala State Civil Supplies Corporation Ltd. (Rs. 1011.02 crores).

**Profitability**

Fifty enterprises have reported profits in 2006-07 totaling to Rs. 816.13 crores as against a total profit of Rs. 308.35 crores earned by 32 enterprises in 2005-06. The remaining enterprises have incurred losses amounting to Rs. 360.05 crores. Nineteen enterprises which had incurred losses during the previous year have reported profits during 2006-07, while one Company which had earned profit during 2005-06 has incurred losses for the year. This puts many serious questions as to the running and management of the undertakings and the cues the private sector players will be deducing from such circumstances.
Employment

The total employment in the public enterprises in the State during 2006-07 was 109934. This is in addition to the indirect employment avenues these undertakings are creating to support their major activities. Barring the statutory corporations, Kerala State Cashew Development Corporation Ltd. alone provides 14702 employment opportunities followed by Plantation Corporation of Kerala Ltd with 2924 and Kerala State Beverages Corporation Ltd. with 2554. However, the average investment per employee during the year 2006-07 was Rs. 16.24 lakhs which was on the higher side when compared with the Central Sector undertakings.

Net Worth

The net worth of the State Level Public Enterprises as on 31st March 2007 was Rs. 1518.92 crores (Rs. 2522.81 crores as on 31st March 2006). It was negative in 34 enterprises at the end of the year. The net worth had eroded fully and become negative in Roads and Bridges Development Corporation, Kerala State Coir Corporation Ltd. Kerala Police Housing and Construction Corporation Ltd. and Kerala Maritime Development Corporation Ltd. Leaving out the statutory corporations, the highest negative net worth was observed in Kerala State Electronics Development Corporation Ltd, The Kerala State Cashew Development Corporation Ltd, Autokast Ltd, Kerala Drugs and Pharmaceuticals Ltd. and Steel Complex Ltd.

Dividend

Nine State Level Public undertakings had declared dividends worth Rs.13.27 crores during the year ending on 31st March 2007 as against 11 undertakings with a
total dividend of 7.93 crores during 2006-07. The Kerala Beverages Corporation Ltd. has reported a payment of Rs. 8.20 crores followed by Oil Palm India Ltd. (Rs. 1.77 crores) and Rehabilitation Plantation Ltd. (Rs. 0.68 crores) on account of dividend for the year. Considering the volume of shareholding interest of the State in these undertakings the figure is very much on lower side which again pinpoints upon the performance level of Public Sector Units of the State 46.

**Comparison with Central Public Sector Enterprises**

In this respect a comparison of the State Level Undertakings with their counterparts in the Centre looks meaningful. Information on the Central Public Sector Enterprises for the year 2006-07 indicates that about 70 per cent of the 225 operating Central Public Enterprises have earned profits. In the case of PSEs in the State, 56.18 per cent of the 90 operating enterprises had earned profits in 2006-07. The return on capital employed in the Central PSEs was close to 12 per cent, while that from the State Level Public Enterprises was negative at 3.58 per cent during 2006-07 (-0.78 per cent in 2005-06). Fifty five enterprises had carried forward losses at the end of March 2006 amounting to Rs. 5706.96 Crores 47. This dismal performance of PSUs, if allowed to continue for sometime can seriously damage the reputation which Kerala tries to project as an industry savvy State. This is to be viewed seriously in the backdrop of the fact that the states like Gujarat, Punjab, Karnataka and Andhra Pradesh are forging ahead with innovative and dynamic business ideas implemented under their respective Public Sectors.
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