Conclusions

The Problem:

The evidence on economic performance of public enterprises is unsatisfactory. These enterprises have caused serious fiscal burdens to the exchequer. They are not generating surpluses and their investment costs are covered by transfers from Government budgets, the banks and financial institutions.

In India, the shortages of foreign exchange have become very acute because of balance of payment difficulties. Public sector will suffer seriously from shortages of raw materials, machines and import components due to inadequate foreign exchange allocation. This is likely to cause under utilisation of capacity already installed and thereby further aggravating the problems of public enterprises.

Deficiencies in project planning have contributed substantially to substandard economic progress. Poor planning resulted in the choice of excessively capital intensive techniques, uneconomic locations of projects, construction delays and poor co-ordination with other industrial aspects of the projects. All these factors made the project sick from its infant stage. Inflated labour force, choice of bad managers because of political patronage, under utilisation of capacities, negligible value-added, all contribute to the ill health of the enterprises and they become prone to
sickness. Lack of competition and protective tariff walls promoted inefficiency manifested in low factor productivity both of labour and capital. Multiplicity of objectives and the weight assigned to non-economic factors also contributed to the poor performance of the public enterprises.

The Profile:

There has been significant growth of public sector enterprises during the various plans. The number of central public sector enterprises in India has risen from a mere five in 1951 to 248 in 1990. Likewise the investment has increased from Rs. 29 crores to Rs. 1,03,000 crores. The stupendous task of developing the infrastructure and the basic and heavy industries was earmarked for the public sector in various Five Year Plans. The Industrial Policy Resolution, 1956, perceived the public sector to occupy "the commanding heights of the economy". The role assigned to the public sector was not based on only ideological grounds but was also necessitated by the prevailing circumstances. Its import substituting role was highlighted in the Seventh Five Year Plan, reducing India's dependence on imports in capital goods sector. In due course of time, the public sector assumed the role of nursing the sick enterprises from the private sector. Its role was diversified into areas other than manufacturing. The other additional responsibilities such as stabilisation of food economy through the Food 340
Corporation of India, Commodity price stabilisation through the Cotton Corporation of India and promotion of foreign trade through State Trading Corporation and Minerals and Metals Trading Corporation were also entrusted to it. Gross Domestic Product amounting to Rs. 24,171 crores was produced in public enterprises during 1980-81 which rose to Rs. 95,392 crores in 1988-89 at current prices. 

The share of public sector to total gross domestic products was 19.74% in 1980-81, which rose to 27.12% in 1988-89. In terms of value added by manufacturing/producing units, they contribute about Rs. 25000 crores to the national output, representing about 8% of GDP. They have made significant contribution in the fields of exploration and exploitation of oil and natural gas, power generating capacity and manufacturing of plant and equipment etc. In addition, they have generated employment, promoted balanced regional development, undertaken measures for employees welfare and fulfilled other social obligations. The public enterprises made very significant contribution in building up the technological and infrastructure base of the economy. The key sectors of the economy are dominated by public enterprises which have successfully expanded production, opened up new areas of technology and built up a reserve of technological competence in a number of areas.
The public investments which were mostly decided in accordance with the Plan priorities till the Third Plan, were influenced by political and other factors thereafter. Efficiency and profitability criteria of public sector were compromised. As a consequence, the public sector became a high cost sector with very low return on the capital invested. Usually a public sector undertaking is envisaged to earn a post tax return of 12% per annum, however, between 1969-70 and 1973-74, gross profits were in the range of 4-6% of the capital employed. During the course of Fifth Plan period, the gross profits ranged between 7-8%. during the Sixth Plan, the gross profits were between 2% to 3% and Seventh Plan less than 4%. The number of loss making units was 103 in 1987-88, 101 in 1988-89, 98 in 1989-90. The amount of loss incurred by these units is mounting. It was Rs. 1745 crores in 1987-88, Rs. 1907 crores in 1988-89 and Rs. 1959 in 1989-90. Only 31 units made a profit between 12-20% in 1989-90. Other units may be termed as implicit loss makers. The public sector enterprises have failed to generate surpluses for development of the economy. Often they have to depend upon Governmental support to carry on with their activities. This has retarded the rate of growth of industrialisation. The enterprises have tended to become a drain on the public finances requiring a net flow of resources to cover their capital requirements.
The rate of return on capital invested is very poor and confined only to a few enterprises like oil companies - ONGC, Oil India Ltd. IOC, IPL, BHEL, MMTC, STC etc. A large number of enterprises are incurring losses. Sector wise the maximum amount of losses are being incurred by steel plants, fertilizers, and transport corporation and of course the taken over sick units like the National Textile Corporation are also waiting losses.

In most of the public sector the cost of investment has substantially mounted because of time overrun, cost overrun and wrong planning. Once the cost of investment is raised in any project, on account of servicing charges, interest and depreciation, the cost of product of the unit goes up perpetually. This is probably the most important factor which has contributed to the high cost economy in our country. Under utilization further aggravates these units.

The products of the public sector are generally of a basic nature used by other industrial enterprises as inputs. On account of the high cost of the public sector products, the cost of other industrial products rises all over the country.
Strategy and Implications:

The public sector assumed an increasingly important role in the industrialisation of our country. We did not set up an appropriate machinery to coordinate and control the activities of the sector. As a result, the sector could not become an effective instrument in the process of economic and social development of the country. In the absence of a well defined strategy, it was impossible for the public enterprises to make a significant contribution.

There is a great diversity and multiplicity of strategies, policies and objectives for development of public enterprises. The role assigned to the public sector has been either promotional, catalyst or developmental in nature. The objective should have been defined at the national level in line with the national strategies and Plans, at the sectoral level to ensure harmonisation, and at the enterprise level to guide management decisions. These strategies were vaguely defined having little relationship to the motives which lead to the establishment of public enterprises initially. The problem was further compounded by the complexity involved in choosing between the commercial objectives and the social objective within the context of the national policy framework.
The changing economic, social and political factors have affected the role, function and organisation structure of public enterprises. In India, the objective of establishing public enterprises was to control, "the commanding heights" of the economic and strategic areas which by their very nature could not be entrusted to private sector.

It is now being realised increasingly that the fulfillment of a set of obligatory indicators of the Plan cannot be the sole objective of public enterprises. Profitability should play an important role in allocation of resources. The signaling role of the commodity and market relations and prices and profits has been increasing even in the centrally planned economies of East Europe. In India, we should adopt a strategy which promotes competitiveness and exports in addition to the rational use of imports. Increased attention must be paid to integrate and harmonise the industrial policy with the development of the agricultural and the treasury sector.

Since the extensive sources of growth have been more or less exhausted, our strategy must focus on getting the best out of the existing enterprises by rationalising their activities and the increasing productivity and efficiency. The basic component of the strategy should be as under:

1) In sectors where the private sector has appeared like manufacturing of cars, the public sector should withdraw.
ii) The social obligations of the public sector should be made explicit and the public sector should be compensated for such social obligations. Placing a value upon social objectives is a subjective exercise fraught with conceptual and technical difficulties. Strong political opposition, also, cannot be ruled out. This will plug any scope for inefficient operation of the public sector. Activities of the enterprise must satisfy the test of economic analysis vis-a-vis the social cost-benefit analysis. It is quite probable that there may be no co-relation between the social and commercial rates of return of public enterprises as was the case of Ghana's public enterprises in 1969 where some of the most profitable PEs owed their existence wholly to very high degree of protection from foreign competition and had negative value added when estimated at world prices.

iii) Because of excessive manning, the public enterprises may have fulfilled the goal of employment generation in the economy in the short term. This has been done at the cost of productivity and efficiency. Redundant manpower makes the operation of the public sector inefficient. The tendency of condoning huge losses of public sector because of distributional goals of Government in providing employment etc., should come to an end. The maintenance of employment level in sick public enterprises is jeopardising the possibilities of creation of many more new jobs in future. A very cautious approach is needed while trimming down the excessive man-power retrenchment, on a massive scale in over-populated countries where job opportunities are scarce, will prove explosive. The labour must be retrained and redeployed in productive pursuits.

iv) Each public sector undertaking should be assigned an export target with a view to make the undertaking internationally competitive. The competitive order is more efficient because it breeds insecurity and almost instantaneous accountability through the ever present threat from the other competitors and the fear of exit. The degree of competition in a market is a good indicator of efficient performance.

v) The loss-making public enterprises which cannot be nursed back to good economic health should be closed down and their salvage value should be utilised to aid the fiscal operations of other units which can be made viable.

vi) Privatisation is not a panacea so long as it does not lead to improvements in allocating efficiency. Allocative efficiency is a function of market structure rather than ownership. It is the function of competitive market. When public owned enterprises compete in the market, economic efficiency can be maintained provided the Government desires such enterprises to remain commercially viable.
The country is facing resource crunch. The implicit losses of profit making public enterprises and explicit losses of loss-making public enterprises need to be put on some footing. The strategy will be for performance improvement through MOU with emphasis on cost effectiveness, higher capacity utilisation, saving in overhead expenditure and input costs, efficient use of working capital and diversification. Efficiency can be improved through the change of market structure from monopoly to competitive wherever required. Only as a last resort where turn around is not possible closure or divestment should be considered to improve the overall picture of public enterprises.

The Policy and Institutional Framework:

There has been no specific policy for improving performance of central public sector enterprises or for tackling sick enterprises. The various measures adopted from time to time relate to organisational restructuring including formation of holding companies, MOUs, increased delegation of powers, emphasis on professionalisms etc. The enterprise specific measures like re-vamping of plant and machinery, voluntary retirement scheme for reduction of surplus staff, capital restructuring, and better management practices, have also been undertaken. These measures have been taken in a half-hearted manner which have tended to be ineffective cures for the long term improvement of the public enterprises. Immediate measures need to be taken
to improve the efficiency and productivity of the public enterprises. Where improvements are not possible, either due to chronic shortcomings or very high cost of re-vamping, options like partial/total divestiture or closure need to be considered seriously.

As a general rule, the enterprises should be required to be economically viable since they are expected to operate on a commercial basis. The social obligations must be separated from commercial objectives. Government should encourage larger self financing by public enterprises. Sound financial management standards and discipline are needed at the enterprise level. The public financial institutions should play more than a mere lending role. They should expand their service function by providing a variety of after sale services. This should include counseling, guidance on financial management and in project preparation etc.

An adequate degree of operational autonomy should be ensured because it is a key element and primary requirement of good management. The operational autonomy of public enterprises must not be curbed. The institutional arrangements of supervision and control should be rationalised. The system should be so designed as to provide for maximum operational autonomy subject to the right pressure of accountability and a balance should be struck between these two requirements. Accountability can be ensured mainly
through an effective system of performance evaluation of the enterprise.

A BIFR like agency for public enterprises can be set up to monitor rehabilitation. This body can formulate rehabilitation packages for the rehabilitation of public enterprises. In addition, the services of agencies like CRISIL, (The Credit Rating Information Services of India Ltd.) should be utilised for proper portfolio management of public enterprises.

The adoption of long-term corporate strategies and plans would go a long way in improving its performance. This should be accompanied by competent leadership dedicated to the cause of the enterprises. The chief executive of the public enterprise should be made accountable provided operational autonomy has been granted to him.

The Scenario

There has been a tendency to understate the importance of financial criteria because of the social directions of public enterprises. This is not desirable. This has led to financial weaknesses of public enterprises resulting in heavy losses. Financially viable public enterprises tend to develop the necessary strength to undertake wider social obligation.
The public enterprises has not been able to utilize effectively their invested resources in terms of efficiency of the use of capital equipment labour and materials. The public enterprises have a heavy degree of capital and labour intensity. Other deficiencies inflicting the public sector enterprises have been - lack of competent top management and leadership, clarity of purpose of the enterprise the relationship between the Government and enterprises and the lack of entrepreneurial ability and initiative to foster the enterprise.

As a consequence the public sector enterprises could not play the role in the national planning process which was expected of them.

Analysis

India was an agrarian economy with a weak industrial base at the time of independence. Vast majority of people were extremely poor having very low level of incomes, savings, and hence investment. There were serious inequalities in income levels and regional imbalances. The infrastructure facilities were almost non-existent. To accelerate the pace of economic development and maintain it in the long term, a big push under the initiative of the State was inescapable to remove poverty and bring about equitable distribution of income ensuring balanced regional development. Public sector was deployed as an instrument of self-reliant economic growth to lay the
foundation of a sound industrial and agrarian base, to overcome the economic and social backwardness. The public enterprises did succeed in achieving a significant degree of self-sufficiency in the critical sector like railways, telecommunications, nuclear power, defence etc.

The actual functioning of the public enterprises has left much to be desired. The key areas which need immediate attention are - generation of adequate internal resources for upkeep of plant and machinery, upgrading of technology, profitability commensurate with size of investment, optimum capacity utilization, reduction in cost of production, proper project planning and management to avoid time and cost overruns, satisfactory marketing and customer services, improvement in quality, over-staffing and the Government and public sector interface i.e. autonomy and accountability, intensive monetary and information system, quick decision making, induction of professional and specialist in the management of the public enterprises, streamlining the procedure for grant of various approvals of the Government to the public enterprise proposals, linking pricing with long term marginal cost of production, and promotion of modality of labour.
Sickness must be detected in time by strict monitoring of production costs. If sickness is detected in good time and the remedy is provided before the malady becomes deep rooted sickness may be easily overcome. A small external stimuli may work as a catalyst for bringing the unit out of sickness. Units located in industrially backward areas are more prompt to sickness because creation of infrastructure facilities adds heavily to the capital cost of the enterprise and it becomes in-competitive and cost of production in such units becomes prohibited. It may be politically and socially desirable but such a move must be supported with infrastructure required for development.

The financial management is also affecting the health of the operating units and manifests itself in lack of financial control, diversion and improper utilization of funds, building up of high inventories etc. This leads to high burden of interest cost affecting the profitability of the unit adversely. The enterprise will be in trouble when the operations require funds. Banks and financial institutions can play a positive role provided the sanctions are issued by them in time. Usually, the sanctions get delayed because of references to their high Head-quarters and to their boards for approval before the funds can be released. This takes good deal of time and the enterprise continues to suffer and incur losses. The
need for proper implementation and monitoring of the turnaround schemes by the companies, institutions, and banks cannot be over emphasised. The concessions like excise, income tax, sales tax, power supply, raw material supply etc. which are granted by Central and State Government must be expedited by the respective authorities. The task of revival of sick units calls for sacrifices from a number of agencies such as - the promoters (that is the Government, in case of Public Sector) financial institutions (i.e., long-term lending institutions) banks, Central and State Governments, and workers. The perceptions of these agencies differ widely and they resist making sacrifices because each agency tries to keep its sacrifice to the minimum. The approach of the agency is more of partisan nature and bringing such conflicting interest together to an agreeable turnaround strategy is a difficult task.

The winding up of a sick unit is a very unpleasant job. These units are kept alive owing to pressure generated on political and social ground. A detailed techno-economic study in each case of the sick public sector unit would be a prerequisite to identify the causes of sickness and prospects of viability. The revival approach has to be confined to potentially viable enterprises and unviable units would have to be closed down. In the face of competition, if a unit is not able to survive, there is no reason why scarce public resources should be continued to be wasted. It will be a wrong policy to keep public enterprises
perennially on artificial respiration. Cases where the cost of the revival of units is more than the cost of setting up similar capacities at green field sites need not be considered for rehabilitation. Revival must be considered strictly on economic grounds. A statutory body on the lines of BIFR will be an effective weapon to counter political pressure because this body would carry out an objective analysis and assessment of the enterprise and if the enterprise is beyond rehabilitation, the exit route would become easier. Therefore, an organisation comprising economists and technocrats should be set up for public enterprises also.

Industrial sickness whether in private or public sector needs to be tackled on priority basis. Time is of essence. The symptoms of the sickness must be identified at the earliest. Techno-economic and commercial consideration should determine the turnaround strategy and not the extraneous factors. A disciplined participative working force adhering to norms and abiding by work culture will prove quite handy in turning around the unit.