Chapter – 5

A CASE STUDY OF VIDESH SANCHAR NIGAM LTD. (VSNL)
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(VSNL)

5.1. Company Background

Videsh Sanchar Nigam Ltd. (VSNL) was incorporated in 1986 as a public sector enterprise to cater to overseas communication services. In 2002, the Indian government privatized VSNL and the Tata Group acquired a controlling stake in the company. VSNL is India’s largest player in international long-distance services and has a strong pan-India presence in domestic long-distance services. The company operates landing stations, undersea cables, Managed services, leased lines and data centres across India. It also runs a network of earth stations, switches and submarine cable systems and offers international telecommunications services including mobile, IP and voice services.

VSNL is the world’s largest international wholesale carrier with more than 415 direct and bilateral relationships with leading international voice telecommunications providers, providing more than 17 billion minutes of international wholesale voice traffic annually. It was the first telecom services provider to acquire the TL 9000 certification globally. The company provides connections to over 400 mobile operators world wide. It is also the principal provider of signalling conversion services to enable GSM roaming to and from North America.¹
a) VSNL Traffic

In 2001, the world international telephone traffic was 167 billion minutes (voice and data, April 18, 2002). India's was 1.6% of this global traffic. In comparison with VSNL, the two largest ILD carriers in the world, world OM and AT & T carried 16.8 and 14.3 billion minutes respectively in 2000. Compared with a world wide average of 145 outgoing international minutes per person, the figure for India works out to 18 corresponding figures for developing countries and low income countries are 100 and 155 respectively (www.worldbank.org). Table 1 compares VSNL's international minutes with that of the world. VSNL during the period averaged a much higher growth rate.

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<table>
<thead>
<tr>
<th>Year</th>
<th>VSNL</th>
<th>World</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994</td>
<td>0.742</td>
<td>54.6</td>
</tr>
<tr>
<td>1995</td>
<td>0.942</td>
<td>61.6</td>
</tr>
<tr>
<td>1996</td>
<td>1.147</td>
<td>71.7</td>
</tr>
<tr>
<td>1997</td>
<td>1.384</td>
<td>82.5</td>
</tr>
<tr>
<td>1998</td>
<td>1.684</td>
<td>93</td>
</tr>
<tr>
<td>1999</td>
<td>1.935</td>
<td>108.9</td>
</tr>
<tr>
<td>2000</td>
<td>2.245</td>
<td>132.7</td>
</tr>
<tr>
<td>AGR 1994 to 2000</td>
<td>20.3%</td>
<td>15.9%</td>
</tr>
</tbody>
</table>

Source: (1) WWW. Telegraph.com
        (2) VSNL Annual Reports
The ratio of inbound to outbound calls had been $4:1$ in 2001. One important reason for this is the discriminatory pricing by VSNL. Another factor is that India is a much poorer than the typical countries to which it connects (US, Europe and Gulf). So that inbound calls are bound to be more than outbound calls. This issue is dealt with in detail in the section on Accounting Rate Reform (ARR). As per industry estimates in India, about $80\%$ of the international telephone traffic was from corporate users for the year 2000-01, the total revenue for VSNL stood at Rs. $64,307$ crore. The profit after tax stood at Rs. $1,778.8$ crore. This resulted in an earning per share of Rs. $62.41$ out of which Rs. $50.00$ was declared as the dividend per share. VSNL had no debt. Its P/E ratio of each VSNL share was $4.68$. It is seen that a large part of the cost is the network and transmission charge. Much of this were charges paid out to the DOT as traffic costs. In this fixed revenue agreement, VSNL paid Rs. $2,734$ crore to DOT and Rs. $1,386$ crore to foreign operators during 2001 (VSNL Annual report 2001).

b) Products and Services

VSNL till recently was the monopoly provider of ILD. It also provides specialized services such as internet, Tr up-linking, direct to Home (DTH) etc. After the recent disinvestments to a strategic partner, the domestic long distance (DLD) sector has also licensed to VSNL. This is however been accompanied by the loss of monopoly in the internet and ILD sectors.

There has been a change in the service pattern of VSNL over the years. Private internet services provides (ISPs) have been expanding rapidly and have overtaken the earlier dominant market share of VSNL
out of the Rs. 2050 crore revenue generated by ISPs, VSNL earned only around Rs. 300 crore in 2001 (www.ispai.com)

c) Investments

VSNL had invested in globally promoted projects like international undersea cables and satellite communications including a sum of US$150 million in ICO global communications (holdings) limited. ICO aimed to provide global mobile personal communication services. On August 1999, ICO filed for bankruptcy and the amount invested has been considered as a write off. Rs. 33 crore were also written off, on account of the failed investments in Iridium’s Indian operations. This was expected to be part of the Iridium satellite system which was planned as a global fully mobile satellite voice and data solutions provider enabled by a set of constellation of 66 low earth orbiting satellite. Due to various problems, the plan never took off. VSNL also held a 2.02% and 5.4% share respectively in Inmarsat and Intelsat. Inmarsat was the world’s largest commercial satellite communications provider and Intelsat has a network of 21 satellite offering telephony corporate networks, Internet and Broadcast services world wide. The majority of international carriers use the accounting rate revenue division procedure promulgated by the International Telecommunications Union (ITU) for revenue sharing for incoming and outgoing calls.
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d) Accounting Rate Reform

There has been a growing imbalance between incoming and outgoing calls in the United States due to interalia to lower priced international calls originating from there. In August 1997, the US Federal Communications Commission (FCC) issued an order establishing benchmarks with which US carriers needed to comply for establishing accounting rates with non-USA carriers (Jan. 2001). As a result, the accounting rate of US carriers with VSNL came down from $0.425/minute to $0.340/minute in 2000-01. In India, international prices did not fall at the same pace. This resulted in increasing imbalance between incoming and outgoing traffic leading to increasing disbursements from the US through the international accounting rates system. US carriers reduced their settlement rates by about 11% after seeking a 25% reduction during 1997-98. That decline was compensated by a revenue increase of 17% in response to rate declines for international calls. Given the size of the payments that needed to be made by the US to India, review of the accounting rate system and its consequents impact on VSNL’s revenue was important. US based companies contributed 38% of the total revenue of VSNL in 2001 (VSNL Annual Report 2000-01), in 1997 VSNL had 64% of its revenue coming in from settlements.

With the opening of the ILD sector, there is a further reduction of rates increasing the outgoing calls to the US and UK. For example, Bharti has already slashed the international tariff to Rs. 24 a minute. This would reduce the income from settlement rate due to VSNL. The revenues of VSNL were expected to experience a downward impact.
following this decision. VSNL had been protected from changes in accounting, settlement and collection rates by virtue of its interconnection agreement with DOT (Later BSNL). The agreement effectively allowed VSNL to retain approximately Rs. 10 per minute for both incoming and outgoing calls since VSNL passed on the balance revenues to DOT as network charges and a decline in accounting rate revenues meant lower revenue surpluses for the DOT. As a part of the privatization package, BSNL and MTNL were required to route their international traffic through VSNL for another two years, contingent on VSNL continuing to offer the best deal available. However, due to rapid development in the sector this policy is not clear as the government had agreed to allow BSNL and MTNL in ILD.

e) WTO

Under WTO’s basic telecommunication agreement by February 2002, nearly three fourths of the outgoing traffic originated in countries that had at least two international operators, while India was to review VSNL’s monopoly in 2004. Under pressure from the WTO, the monopoly was removed in 2002, with the removal of restraint on ILD, any communication consortium could set up landing points in India and go in for direct agreements with basic land line operators. This meant that VSNL would lose any privilege it might have had as a dominant player in the Indian segment. It was also expected that in the liberalized market atmosphere in the wake of WTO imposed situations. The present complex system of accounting and settlement rates may be replaced by cost sharing on a market dictated basis.
## Table-24
Share Capital History of VSNL

<table>
<thead>
<tr>
<th>Dates</th>
<th>Particulars</th>
<th>No. of New Shares</th>
<th>Total No. of Shares</th>
<th>Nominal Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>19.03.86</td>
<td>Allotted as purchase consideration for assets and liabilities of OCS</td>
<td>126</td>
<td>126</td>
<td>1,26,000</td>
</tr>
<tr>
<td>01.04.86</td>
<td>Allotted as purchase consideration for assets and liabilities of OCS</td>
<td>5,99,874</td>
<td>6,00,000</td>
<td>600,000,000</td>
</tr>
<tr>
<td>March 91</td>
<td>Shares of 1000/- each subdivided into shares of 10/- each</td>
<td>-</td>
<td>60,000,000</td>
<td>600,000,000</td>
</tr>
<tr>
<td>06.02.92</td>
<td>Bonus of 1 : 3 issued to Govt. of India</td>
<td>20,000,000</td>
<td>80,000,000</td>
<td>800,000,000</td>
</tr>
<tr>
<td>Jan-Feb. '92</td>
<td>12 million shares divested in favour of Indian Financial institutions by GOI @ 123/share</td>
<td>-</td>
<td>80,000,000</td>
<td>800,000,000</td>
</tr>
<tr>
<td>1994-95</td>
<td>2,362,529 shares transferred to divested parties as bonus shares</td>
<td>-</td>
<td>80,000,000</td>
<td>800,000,000</td>
</tr>
<tr>
<td>27.03.97</td>
<td>VSNL raised its share capital by way of GDR issue and also GOI divested in GDR markets @ US$ 13.39 per GDR equivalent 1000/- per share</td>
<td>12,165,000</td>
<td>92,165,000</td>
<td>921,650,000</td>
</tr>
<tr>
<td>04.04.97</td>
<td>VSNL raised its capital by way of GDR issue green shoe option @ US$ 13.29 per GDR equivalent 1000/- per share</td>
<td>2,835,000</td>
<td>95,000,000</td>
<td>950,000,000</td>
</tr>
<tr>
<td>Feb. 99</td>
<td>10,000,000 shares divested by GOI in GDR markets @ US$ 9.25 per GDR equivalent to 786.25/- per share</td>
<td>-</td>
<td>95,000,000</td>
<td>950,000,000</td>
</tr>
<tr>
<td>May 99</td>
<td>3,96,991 shares divested by GOI by way of offer of shares to employees of VSNL @ 294/- per share locked in for a period of 3 years.</td>
<td>-</td>
<td>95,000,000</td>
<td>950,000,000</td>
</tr>
<tr>
<td>Sept. 99</td>
<td>1,000,000 shares divested by GOI in Domestic markets @ 750/- per share</td>
<td>-</td>
<td>95,000,000</td>
<td>950,000,000</td>
</tr>
<tr>
<td>15.08.00</td>
<td>Listing of ADR’s on NYSE</td>
<td>-</td>
<td>95,000,000</td>
<td>950,000,000</td>
</tr>
<tr>
<td>24.11.00</td>
<td>Bonus shares in the ratio of 2 : 1</td>
<td>190,000,000</td>
<td>2,850,000,000</td>
<td>2,850,000,000</td>
</tr>
</tbody>
</table>

Source: VSNL Annual Report (2000-01)
Table-25

VSNN Stock holding pattern as of March 31, 2001.

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Category</th>
<th>No. of Shareholders</th>
<th>Voting Strength</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Central Government including nominees of the president of India</td>
<td>3</td>
<td>52.97</td>
</tr>
<tr>
<td>2.</td>
<td>Indian Public Financial Institutes and Mutual Funds</td>
<td>64</td>
<td>6.78</td>
</tr>
<tr>
<td>3.</td>
<td>Indian Nationalized Banks</td>
<td>13</td>
<td>0.08</td>
</tr>
<tr>
<td>4.</td>
<td>Foreign Financial Institutions</td>
<td>137</td>
<td>7.82</td>
</tr>
<tr>
<td>5.</td>
<td>Foreign Companies (shares held by Bank of New York or depository for ADRs</td>
<td>1</td>
<td>29.22</td>
</tr>
<tr>
<td>6.</td>
<td>Non-resident individuals</td>
<td>202</td>
<td>0.02</td>
</tr>
<tr>
<td>7.</td>
<td>Other Indian Corporate Bodies</td>
<td>1,548</td>
<td>0.68</td>
</tr>
<tr>
<td>8.</td>
<td>Others (including employees)</td>
<td>66,303</td>
<td>1.96</td>
</tr>
<tr>
<td>9.</td>
<td>In transit demat shares</td>
<td>-</td>
<td>0.47</td>
</tr>
</tbody>
</table>

Source :- VSNL Annual Report (2000-01)

f) Domestic Developments

The central government’s policy of disinvestments has evolved over the last ten years. It started with the selling of minority shares in 1991-92 and today continues with the emphasis on strategic sale (Bajjal 2002). Many of the government owned PSUs were known to be inefficient. Many others with their commercial profits may also not have been efficient owing their profits to either their monopoly positions or administered prices, such secure arrangements were no longer possible with the WTO related agreements for opening up of several sectors coming in to force.
The ministry of disinvestments cited the non-availability of funds for critical areas like education, health and social infrastructure because of fiscal burden in the flow of government funds to PSUs, as a strong argument for the disinvestments. There was also a need to stem further outflow of resources into unviable, non-strategic PSUs. The disinvestments was also expected to reduce the unmanageable public debt.

Distributing government held stock to the public can help investors to directly enjoy the benefits of ownership. Even as their pressures helped to improve performance. However, the perception was that such an approach did not usually bring about efficiencies and effectiveness in management as it was usually not accompanied by management change. Strategic sale was viewed as a way to increase the valuation of a company and also to bring in private capital and managerial acumen into the organization. Importantly, it was also necessary to separate the policy making and operational responsibilities of the government, which otherwise caused a clash of interest and an unhealthy environment for competition. Especially in areas of infrastructure that required some kind of regulation. This approach paved the way for the political acceptance for the strategic sale of VSNL.

5.2. Prior Disinvestments

When the privatization process of VSNL began in 1991-92, there was no blueprint for the same. In retrospect, there have been three phases (1) the offloading of shares to domestic investors (2) the offloading of shares in the international market (3) strategic sale.
In 1991-92 VSNL disinvested equity of the face value of Rs. 12 crore in favour of various financial institutions, banks and the public held another 15%. The shares were listed in the stock exchanges of Mumbai, Kolkata, Delhi and Chennai. As of 1995, the share of the GOI had come down to 82.02%. This accompanied the transfer of shares from the GOI as a bonus offer. The Indian investors share holding remained around 16.5% in 1999-2000 which came down to 9.97% as on March 31, 2001.

5.3. GDR Issue

The Global Depository Receipt (GDR) issue for VSNL was the first of its kind by the GOI. It helped VSNL to raise a substantial surplus that was earmarked for investments for its Growth. The first GDR issue (Listed on the London stock exchange) was offered in 1996-97. It fetched US$526.6 million in the market. At that time, it was the largest GDR issue from India. The offer was oversubscribed, drawing 662 investors from 28 countries.

The second GDR issue was completed in February 1999. It involved disinvestments of 10 million shares by the government of India to international investors. Priced at US$9.25, it was at a 15% premium on the last closing domestic price of Rs. 682 and a 10% discount to the ten-day average GDR price of US$ 10.275. The government realized US$ 185 million from the sale of 20 million GDRs with each GDR being equivalent to half a share.

The organizational problems in VSNL around the time of the second GDR issue could have been one of the factors that led to lower valuations. During the process of the second GDR issue, the VSNL staff
had threatened a walkout owing to the pending issue of allotting shares to employees. Due to delays in the government processes, VSNL did not have a chief executive and many other crucial director level posts were vacant. The first GDRs investment promises were not fulfilled and a promised domestic offering had not been made. The sanctions against India also created an environment of high perceived country risk which lowered VSNL's valuation.

5.4. Sale of Strategic Partner The Valuation

The government had fixed a reserve price of Rs. 1,218,375 crore for its 25% stake in VSNL. In an effort to bolster the VSNL valuation, the government of India limited (GOI) intended to compensate the loss of monopoly through special concessions. The government owned MTNL and BSNL would have to use VSNL as their ILD carrier for two years on the condition that it would offer the most competitive terms in the market. VSNL would also get a free license to provide NLD and a nationwide ISP license. In addition VSNL possessed prime real estate in Mumbai and Delhi and also cable capacities to facilitate international traffic. One of the major assets was the cash stock pile of Rs. 5,182 crore which was considerable even after disbursement of the special dividends. Among the concerns were the loss of monopoly and the uncertainty of the loyalty of BSNL and MTNL to continue to use VSNL for their international traffic, the dipping share prices of VSNL and the falling accounting rates that could lead to lower revenues.

One of the major issues involved during the valuation process included the management of real estate owned by VSNL. The disinvestments process stipulated that at least four VSNL surplus
properties valued at Rs. 778 crore would not be available and were to be disassociated from VSNL after the disinvestments. Even so, real estate value that would accompany. VSNL was around Rs. 1,200 crore. (Economic Times, February 15, 2002).

For the government going in for a strategic sale was better than the previous market offloading option as strategic investors were likely to pay a higher price than financial investors. There was also a pressing need to bring in a fresh, market oriented approach to the organization in the changed economic situation. As stated by the former union disinvestments minister Arun Shourie, VSNL had reserves of about Rs. 4500 crore with a ‘bank check’ given by the cabinet to enter new businesses and prepare for the loss in monopoly. The fact that it had failed to do so was a clear indication of the lethargic decision-making and the constraints of continuing to be a state owned enterprise. The sense of urgency given the potential loss in value, due to the annulment of its monopoly status and the threat of internet telephony ensured that the government acted promptly in executing the disinvestments process.

5.5. The Bidding Process and after

Companies, joint ventures and consortia interested in participating were required to have a net worth of Rs. 2500 crore. The net worth of only those promoters was to be counted who had more than a 10% equity stake in the total equity of the company. The SEBI takeover code required that the strategic partner would come out with an open offer for an additional 20% stake. The strategic partner was expected to bring in expertise and managerial acumen.
The bid was open to international parties but did not draw any interest because of the 49% capital of foreign direct investments in the telecom sector. GDRs and FIIs already accounted for 38% of VSNL’s equity capital that left only a remaining 11% for the foreign company. This left out foreign firms like MCI world com, France Telecom, Telecom Italia, BT and AT & T, who had shown interest earlier among the domestic players, the initial 7-8 players who showed interest were paired down to Reliance and the Tata Group by the time the bidding process began. In choosing between prospective strategic partners, the government way to pay due attention, interalia, to the security requirements of the country.

The Reliance Group Bid Rs. 1,347 crores, loosing out to the Tata Group bid of Rs. 1439 crore. The Tata bid for the 25% stake worked out to Rs. 202 per share as against the then prevailing market value of Rs. 168 per share. The total realization from VSNL was expected to fetch the government Rs. 3,689.25 crore after factoring in Rs. 1,887 crore as dividend and Rs. 363 crore as dividend tax. The Rs. 1300 crore required for the extra 20% stake were obtained through zero coupon non convertible debentures backed by guarantees from Tata sons and Tata power. After disinvestments and the acquisition of equity by the Tatas, the government share had dropped to 26%. The Tata group had 45% and an extra 1.97% had been disbursed to employees. Most of the Tata acquisition of 20% stake in the open market came from the foreign holders.2
5.6. Tatas Hit Jackpot with VSNL

The Tata group seems to have hit a jackpot by acquiring strategic stake in Videsh Sanchar Nigam Limited (VSNL). According to analysts, with one stroke, it will be able to be a dominant player in the International Long-Distance (ILD) and internet services, even as it is readying to make a foray in the National Long Distance (NLD) segment. The group already has a presence in the cellular and the basic services, making it the first fully integrated telecom player in the country.

While its rival in the VSNL bid - Reliance has for long been talking of being the first such player in the Indian market, its ground operations are yet to take off. It has a limited basic and cellular network, which is operational, its internet, NLD and ILD services have not yet seen the light of day.

Bharti, the other big player, does not have presence in the ILD segment, having opted out of the race for VSNL a couple of months ago. It does have a sizeable cellular and internet presence, even while its basic and NLD operations are in the take-off stage. Analysts noted that having acquired control over VSNL, the Tata group will now be able to synergize all its existing operations even as it can cut cost by availing itself of the concessions being granted by the government for early termination of the monopoly on ILD services.

The financial benefits given to VSNL include a five year reimbursement of license, entry and revenue sharing fees and exemptions from performance bank guarantees, all which the Tata group will get. What is more, VSNL has also planned to go full steam ahead with its NLD services, instead of picking up a license for the
same, the Tata group can now avail itself of this shortcut. The group had earlier made a tentative investment of Rs. 1000 crore, for rolling out these services. This could now be scaled down considerably.

As regards basic services across the country, at present it offers the services in Andhra Pradesh, and is due to roll out new operations in the four circles of New Delhi, Gujarat, Tamil Nadu and Karnataka. Meanwhile in the internet segment, it was earlier proposed to merge Tata Internet Services Ltd. with its basic services operation. This was being considered in the light of the plans for offering broadband services in all its circles of operations.

However, since VSNL is the market leader in this business with a share of about 50 percent in the major cities, the internet services of both these companies could be merged.

VSNL already has a ready internet subscriber base of 6.6 lakh, having rolled out ISP services in the four metros and its own internet nodes at 18 cities. The Tata internet services network is now present across 32 cities in the country.

5.7. VSNL Enters Tata Family

The Tatas formally acquired 25% equity stake in Videsh Sanchar Nigam Ltd. (VSNL) by signing the shareholder's agreement with the government.

Mr. Ratan Tata, Chairman of the Tata Group, handed over a cheque for Rs. 1,439 crore to Mr. Pramod Mahajan, Union Minister for Parliamentary Affairs, Information Technology and Communications. The Tatas can now have four directors on VSNL's reconstituted board. They are Mr. Ratan Tata himself as VSNL's non-executive chairman,
Mr. S.K. Gupta, reaffirmed as VSNL’s managing director and Mr. N. Srinath, CEO, Tata Internet, who joins as executive director.

Mr. Tata at the first board meeting of VSNL said disinvestments at VSNL was “a vindication of the government’s intent to privatize major companies”.

VSNL will be integrated into the telecom plans of the Tatas “we will develop those synergies over the next few days or weeks. By and large, we will try to find synergic solutions”, Mr. Tata said when asked how he proposed to handle the separate internet services of VSNL and Tata Nova. Speaking to newsmen after signing the agreement, he said that a committee would be set up to oversee the larger process of integrating VSNL. From the Tatas’ side, Mr. Srinath may head the committee. There are no plans to introduce any Voluntary Retirement Scheme (VRS) at VSNL. In a presentation on the telecom sector, Mr. Kishore Chauker, Managing Director, Tata Industries, said that the Tatas aimed to capture a significant market share of the 25 million subscribers in the private sector from a total base of 85 million forecast for 2006.4

a) 10-lakh Block Deal

VSNL shares registered an increase in volumes as well as price on the bourses. Total Shares traded on the Bombay stock exchange after the disinvestments of VSNL were 21.46 lakh and on National Stock Exchange (NSE), traded volumes were 21.76 lakh shares, up from 6.35 lakh shares. A dealer said there was a block deal of 10 lakh shares on BSE other deals were of smaller quantities.
b) The New Board

VSNL has informed the Bombay Stock Exchange of reconstituted board. According to its statement, the new board consist of Mr. Ratan Tata - Chairman, Mr. S.K. Gupta - Managing Director, Mr. N. Srinath - Director (operations), Mr. Sadhana Dikshit - Director, Mr. Rakesh Kumar - Director and Mr. N.R. Narayana Murthy - Director.

Mr. Rajneesh Gupta, Director (Network) and Mr. R.S.P. Sinha, Director (Finance) have resigned.

"The holding of the Government stands reduced to 27.97 percent", the statement said.

c) The TTL Controversy

The controversy over the TTL investment began when the VSNL board (under Tata management) decided to invest Rs. 1,200 crore in TTL. The Tatas justified the decision being part of the effort to extend VSNL’s activities to the basic services customer. The investment was to be made over 3-4 years for a 20-26% stake in the company. TTL was planning projects worth Rs. 8,247 crore over the next four years with equity amounting to Rs. 4,325 crore. Out of this, the Tata group was to put in Rs. 2,552 crore, VSNL was to put in Rs. 1,200 crore and Rs. 573 crore were to come in from non Tata sources. The union communications minister (Mr. Pramod Mahajan) objected to the decision. To him it was unethical that the Tata group was using up cash reserves of VSNL to fund its own subsidiary. In minister’s perspective, TTL was a new company that was yet to prove itself. In his opinion, if VSNL wanted investment in basic services, BSNL and MTNL might provide better opportunities. The ministry had threatened legal action if
it were not able to persuade the VSNL board to reverse the TTL decision. The government also had the option of forcing VSNL to pay dues worth Rs. 1,050 crore to BSNL as pass through charges for using BSNL's network. The ministry of communications (MOC) as well as some other sources felt that VSNL's investment in TTL was based on an over valuation.*

The Tata led management has decided to sell 75% of its holding in Intelsat and 100% of its holding in Inmarsat. The revenue from Intelsat/Inmarsat for the year 2000-01 was Rs. 115.6 crore. The sale of stock in these companies is expected to fetch VSNL Rs. 1200 crore. Apart from the realization of this amount from the sale, the Intelsat-Inmarsat sale is also expected to help open other competitively priced options for VSNL for meeting its satellite communication requirements. Others are 2.6% in Netherlands passed New Skies satellite NV, IOCOM cable (Chennai-Penang), South-East Asia - Middle East-Western Europe 2 (SE-ME-WE-2) optic fibre connecting 14 countries of the regions, and the SE-ME-WE 3 cable that connect 39 countries.

After some deliberations between the MOC and VSNL, the government had indicated that if a higher stake of around 50% in TTL were to be available (at the same price) then it would not have any objection to the investment.

Legally though, the Tata group was well within its rights to move. According to the companies Act, strategic partners were free to utilize cash reserves of public sector units. The disinvestments ministry also did not foresee any future change in the shareholders' agreement with respect to use of company reserves. The unnecessary spat that
developed led to a drop in the share price of VSNL from 188 on May 28, 2002 to 161 on June 10, 2002.

d) Issues on Disinvestments

1. Does Disinvestments Lead to a More Efficient Public Expenditure

During the last two years of strategic disinvestments, only 1% of the government's equity of face value Rs. 744 crore had been sold. The government had recovered Rs. 7,164 crore from these sales. Government of India's borrowing rate is 10%. Hence, this realization would lead to a benefit of Rs. 721.96 crore to the country every year in perpetuity. As against this benefit, the dividends received by the government on its equity, which had been sold, averaged Rs. 23.17 crore during the last eight years. However, some of the companies were loss-making, leading to an overall outgo of Rs. 102.83 crore from the government for the maintenance of its PSUs. This worked out to an annual real benefit to the economy to the tune of Rs. 721.96 crore. In the case of VSNL, the government had been receiving Rs. 10.4 crore as dividends (average of eight years upto 2000) from VSNL.

The sale of 25% stock resulted in an inflow of 3,689 crore (including the special dividends) leading to an earning of Rs. 368.9 crore in perpetuity (as interest on 10% deposit annually). Viewed from this perspective, the privatization has led to a better expenditure management. It may be argued that by the privatization process, the government had lost claim on its assets or shareholding. But this may be compensated by the higher cash returns generated from the sale.
Moreover, service quality and prices, and efficiency can improve for the consumers and citizens.

2. Public Issue Versus Strategic Sale

Before the year 2000, the government was selling minority shares in VSNL. The price to earning ratio was 6.0 at that time. The strategic sale gave a much higher price to earnings ratio of 11.0. This was an indication of the market expectation of better performance under a private management. However, it is not always true that strategic sale alone leads to better valuations. In the case of British Telecom’s (BT) privatization that was done through sale of shares to the public, the government made significant changes in the board membership to indicate the greater business orientation the future privatized BT was likely to have. The Indian government could have brought in greater accountability of performance in its PSUs and specifically VSNL even prior to privatization by implementing similar changes. In the absence of such changes, VSNL’s share prices could not gain from IT/telecom boom. A more proactive approach to managing VSNL even before privatization would have increased the valuation of VSNL and led to better public expenditure accountability.

3. Valuations

Critics of the present process of disinvestments have pointed out that many PSUs have been sold below their actual value. They also point out that short term perspective of reducing the fiscal deficit should not drive the process of privatization. The claim of privatization boosting share prices of PSUs had also been proved wrong by the case of VSNL. The advisors and professionals who assist the ministry of
disinvestments may not be entirely disinterested parties either. This could lead to improper evaluation of the PSU and its bidding process.

In addition, there are several steps that the government or VSNL board could have taken prior to the privatization to increase its valuation. But a lack of accountability to the citizen, led to a situation where VSNL was functioning with out a CEO and senior officials, highly undermining the share prices and losing out on initiating strategic businesses such as domestic long distance. Often, the DOT thwarted VSNL's business plans. For example, VSNL was not given a nation wide ISP license or a domestic long distance license. This prevented both DOT (now BSNL) and VSNL from learning about how to deal with competition and starting into new business areas.

**Government Role**

Even after a strategic sale, it is the government's responsibility as a shareholder, to ensure that such enterprises are allowed to function smoothly without interference from politicians. The Tata Tele services (TTL) controversy highlights the difficulties it faces in doing so. Although the government's role in privatized PSUs in ensuring public expenditure accountability is clearly reduced, it could continue to be significant. The MOC as a stakeholder had the right to question the investment decision vis-à-vis TTL. But this should have been done through the decision making structures and committees within the board and not subsequent to the decision.

The government seems to be taking an ad-hoc view by not having a clearly set out action plan. For example, it is not known how long the government plans to retain the 26% stake.
Conclusion

The disinvestments of VSNL is seen as leading to public expenditure accountability through a realization of higher return on the government’s asset formation. It also leads to an appreciation of the remaining shares that are held by the government. To the citizen, the process is a step towards the provision of better quality communication services at the most competitive prices.

Public flotation of stock might have led to better values for VSNL’s stock, had the company been correctly ‘prepared’ for privatization. Considering that such a process was not underway, the present route of strategic sale seems an appropriate option.

e) Summary of VSNL Disinvestments

VSNL Disinvestments

- Profitable, Cash Rich - Navaratna
- Had Monopoly in ILD, Internet.
- WTO Stipulations led to loss of monopoly
- Strategic sale in April 2002
- Tata’s holding – 45%
- Government’s holding – 26%
- Concerns over Rs. 1200 crore investments in Tata Tele services.

Events Leading to Disinvestments

- Domestic Developments
  - Minority Shares’ sale in 1991-92
  - Strategic sale considered better than minority sale.
- Pressure due to WTO agreements
- Government keen on reducing burden of running PSUs.
- Sale proceedings to reduce public debt.
- In 1991-92, VSNL first disinvested.

Prior Disinvestments
- Offloading to domestic investors.
- Offloading of shares in International Market
- Strategic Sale

GDR Issues
- First issue fetched US$526.6 million (1996-97)
- Second issue fetched US$185 million (1999)

**Sale of Strategic Partner**

- The valuation
  - Reserve Price of Rs. 1218 crores for 25% stake.
  - MTNL, BSNL to use VSNL for 2 years.
  - NLD license thrown in
  - Cash stockpile of Rs. 5182 crores.
  - Some prime real estate not included in deal.
  - Potential loss of value led to Urgency.

- The bidding process and after
  - SEBI takeover code needed bidder to purchase 20% post bidding.
- Tata bid Rs. 1439 crores, Reliance bid Rs. 1347 crores
- After takeover, Tatas - 45%, Govt. - 26%
- 1.97% given to employees.

- The TTL controversy
  - VSNL boards decided to invest Rs. 1200 crores in TTL
  - Over 3-4 years for 20-26% stake

- Tata’s justifications
  - Extend VSNL’s reach to basic services.
  - Part of Tata group’s overall telecom strategy.

- Communication Minister’s objection.
  - Unethical to use VSNL’s cash reserves.
  - BSNL, MTNL might provide better investment opportunities.
  - TTL might have been overvalued

- Issue resolved
  - VSNL board sets up a committee to review the quantum and valuation of the proposed investment.

- Result of TTL Controversy
  - Government had made bad decisions in the past (ICO, Iridium)
  - Legally, Tata was well within its rights.
• Issue could have been handled better by better information availability to 26% share holder (government)

• Bad publicity – share prices fell from Rs. 188 on May 28, 2002 to 161 on June 2002.

Issues on Disinvestments

• Does disinvestments lead to more efficient public expenditure?
  • Compare perpetual returns (with 10% annual rate) due to government. PSU sale realization against dividends received (722 crores versus 23 crores).
  • For VSNL (including special dividends), perpetuity amount is Rs. 369 crores whereas dividends were Rs. 10.4 crores.

• Public issue versus strategic sale
  • During disinvestments period, price/earnings (P/E) was 6.
  • Strategic sale gave price/earning of 11.
  • Market expects more from private management.
  • Better Management in the past might have led to more valuation and therefore greater performance accountability.

• Valuation
  • Critics claim sale below actual value.
- Share prices did not go up as expected.
- Advisers and professionals might not be disinterested parties.
- Lack of accountability (Vacuum in top management for a long period).

Government’s Role

- Even after sale, government has responsibility as a shareholder to ensure smooth functioning.
- Ministry of communication’s questioning might be right, but should be through decision-making structures and not in public.
- Government should learn to ‘let go’
- Road Map for the remaining 26%?

f) Conclusion

- Disinvestment of VSNL led to greater Public expenditure accountability through higher return on government’s asset formation.
- Better quality communications for the citizen.
- Strategic sale is good as it leads to less confusion among the government’s roles as a policy formulator and a service provider.

5.8. VSNL Performance after Disinvestments

1. VSNL, a member of the US$29 billion Tata Group, is a leading global communications company offering next generation voice, data and value-added services to enterprises carriers and retail
consumers. Voted the best wholesale services provider at the world Communications Awards, 2006, VSNL is one of the largest providers of wholesale International voice services and operates one of the largest global submarine cable networks, VSNL’s customer base includes 1500 global carriers, 450 mobile operators, 10,000 enterprises, 100,000 broadband and internet subscribers and 300 wi-fi public not spots. VSNL has offices in over 35 countries including the United Kingdom, South Africa, Singapore, Hong Kong, Sri Lanka and India. VSNL’s global transmission network of over 2,00,000 route kilometers and its IP core with 200 points of presence enable a range of services that include voice, private leased circuits, IPVPN, internet access, global Ethernet, hosting, mobile signaling and other IP services.

VSNL (www.vsnl.com) is listed on the Bombay Stock Exchange and the National Stock Exchange of India and its American Depository Receipts (ADRs) are listed on the New York Stock Exchange.

2. VSNL’s Executive Director, Mr. N. Srinath has been named the ‘Telecom CEO of the Year’ by the leading publishing group, Telecom Asia in the 2006 edition of their awards.

The 2006 Telecom Asia award has been given in recognition of Mr. Srinath’s role in transforming VSNL from a domestic monopoly to a major global telco in just four years. This makeover was achieved at a time when the Indian telecommunication market was becoming de-regulated and fiercely competitive.
3. In 2005, VSNL acquired Tyco global network, a state of the art undersea cable network that covers Europe.

4. On February 14, 2006, VSNL completes acquisition of teleglobe International Holdings Ltd. The new combined company will own and operate one of the world’s largest International mobile, data and voice networks with coverage to more than 240 countries and territories, with its acquisition of teleglobe, the company’s wholesale customers will benefit from superior network reach and scalability from a single partner worldwide for voice, data and mobile services.

5. On July 31, 2007, VSNL launches next generation dedicated global Ethernet services for the Australia Market. Metro Ethernet Forum (MEF)9, and 14 certified Global Ethernet Services enables Australian enterprises to connect to India and throughout the world. The Metro Ethernet Forum is a global industry alliance that develops Ethernet standards with the cooperation of over 120 companies worldwide including telecommunications service providers, cable MSOs, Network /Equipment Software manufacturers, semi conductors vendors and testing organization.

6. VSNL has been chosen as the network administrator for one of the world’s largest and sophisticated, trans-continent cable systems - SEA-ME-WE4 (South East Asia - Middle East - Western Europe). This is the first time that an Indian company has been chosen as the network administrator for a global
consortium cable system. The SEA-ME-WE4 consortium has 16 members.

VSNL also hosts the network operating centre in Mumbai. The twin role of network administrator and hosting the operating centre will enable VSNL to play a key role in the day to day operations of the cable system.

7. Tata Indicom wi-fi services at Eden Gardens. Tata Indicom wi-fi service will eventually roll out 1000 hot spots all over India and is already providing its services at some airports, hotels, stadiums and restaurants, wireless fidelity (wi-fi) enables computers, PDA's and other computing devices to use high speed internet without the need for any wires or cables. This services can be availed at places which wi-fi enabled and in common parlance called “Hot Spots”

8. Currently, the company has 52 subsidiaries in 21 countries as well as operations across four continents. VSNL International a subsidiary of the company, takes care of its international operations. It has its offices in Virginia, New Jersey, London, Paris, Madrid, Amsterdam, Frankfurt, Singapore and Tokyo. Its ADRs are listed on the New York Stock Exchange.8

5.9. VSNL International

VSNL International, the Internations arm of Videsh Sanchar Nigam Limited is a leading global communications services provider offering a comprehensive portfolio of next generation carrier and enterprise solutions, including Voice, mobile, data and Ethernet. VSNL International owns and operates one of the world’s largest international
mobile, voice and data networks providing global reach to over 240 countries and territories. In addition, VSNL international owns’ the world’s largest designed global backbone capacity network, spanning across 4 continents and comprises of Major ownership in 206,356 km of terrestrial network fibre-optic networks and sub-sea cables. It is also one of the largest carriers of wholesale voice globally.

VSNL and VSNL International are a part of the Tata group, a $29 billion global conglomerate comprising 93 operating companies, VSNL International is headquartered in Singapore with regional offices in the North America, Europe and Asia pacific. VSNL International had a work-force of about 2000 employees.

5.10. Factors for success

VSNL has a world class infrastructure, it offers multiple connectivity options internationally, using its robust network infrastructure. It operates a total of 26 switches 5 international gateway switches and 21 national long distance switches worldwide. It has over 50 earth stations and terrestrial cable systems with 2,00,00 kilometers of fibre and cable. The company offers high-end services to its EU clients by successfully leveraging infrastructure.9

Conclusion

From the foregoing analysis, it is observed that the VSNL a cash rich public sector enterprise has become from ‘Good’ to ‘Better’ enterprise after disinvestment. A comparative study of EBITDA of VSNL before and after disinvestment is given below, which further justifies the above statement.
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### EBIDTA of VSNL After Disinvestment

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1. www.vsnl.com
5. i Economic Times, February 15, 2002 “ Tata’s get Rs 1300 crore worth of property with VSNL deal”
   ii Bajaj, Pradip, Economic and Political weekly, April 27, 2002
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