Chapter – 6

CONCLUSION AND RECOMMENDATIONS
6.1. Findings and Conclusion Pertaining to Disinvestment Programme in India

In a mixed economy such as India, public sector had been assigned an important role. They were considered 'Temples of Modern India'. These temples were built during socialist Indian politics and planned economy. However, in the year 1991, due to balance of payment crisis and budgetary deficits the national economic policy underwent a radical transformation. The new policy of liberalization, privatization and globalization de-emphasized the role of the public sector in the nations' economy. It is also contended that the functioning of many public sector units has been characterized by low productivity, unsatisfactory quality of goods, excessive manpower utilization, inadequate human resource development and low rate of return on capital. For example, between 1980 and 2002, the average rate of return on capital employed by PSUs was about 3.4% as against the average cost of borrowing which was 8.66%. Disinvestment of the PSUs has therefore been offered as one of the solution in this context. Disinvestment means withdrawing investment or reduction of investment which occurs by selling of equity and bond capital invested by the government in public sector units to private sector. This in turn would enable the much needed revenue generation by the government and help reduce deficit financing. Since the sale of the state owned assets are highly visible projects in India's political economic life. Disinvestment are treated with great caution and care by the
government to do it right. After the initial round of disinvestments in 1991-92, the process has been guided by recommendations made by a committee on disinvestments set up in 1993. Further, in 1996, the government constituted an independent body called the disinvestments commission to design and execute the privatization of the public sector units. To ensure a high degree of transparency of the deals, the commission submits all documents and papers regarding every disinvestments case to the office of Comptroller and Auditor General (CAG). The CAG office will then prepare a thorough assessment and send it to parliament before releasing it to general public. Thus, in some cases, the government seeks the parliament’s prior approval for the execution of the deal. Although there is a three-tier mechanism for decision making and implementation of disinvestments yet the basis of selection of an enterprise for disinvestments is still not clear.

The government has adopted two methods of disinvestments over the period 1991-92 to 2006-07 (i) first method adopted was partial disinvestments whereby the government still retained effective control by holding 51% or more of equity. This method was used in majority cases over the period 1991-92 to 1998-99. (ii) second method is strategic sale with complete transfer of management of a public sector unit to a private sector company. Since 1999-2000 the emphasis shifted to the latter method. Modern Food Industries Ltd. (MFIL), BALCO, CMC, HTL, IBP, VSNL, Pradeep Phosphates Ltd, HZL, IPCL and Maruti Udyog Ltd., were sold off in this manner.

The public sector employment has come down during the post reform period due to economic pressures. There has been a uniform decline in growth rate of employment among all state owned
enterprises during this period. Therefore, the fear that disinvestments would severely undermine employment is largely exaggerated.

The objectives of disinvestments have not been precisely stated. However, based on budget statement, it can be inferred that the objectives sought to be achieved are fiscal discipline and improvement in efficiency. Although, encouraging wider public participation in the disinvestments programme was initially an objective, it was dropped later and the strategic sale route was followed. By following the strategic sale route higher realization has been achieved, but the public has been excluded from the process. Whether this yield of higher return in the short run will benefit the public in the long is debatable. The current declared policy is that the government is prepared to reduce its stake in the non-strategic PSEs to even below 26% if necessary. However, rationale of retaining minor share holding in a non-strategic public sector enterprise is debatable. The Government can realize better price while undertaking 100% sale and no useful purpose is served by retaining a minority holding in a non-strategic sector. The interest of workers can be safeguarded through shareholder agreement even in a 100% sale.

However the performance on the disinvestment front over the period 1991-92 to 2006-07 has been dismal. The value of the disinvestments realized in the past years have fallen far short of their target. During the period 1991-92 to 2002-03, the Government had targeted the mobilization of about Rs. 78,300 crores through disinvestment, but from 1991-92 till may 2007 the central government has raised just Rs. 51,609 crore from disinvestments transactions with the highest receipts of Rs. 15,547 crore realized in 2003-04 through
strategic sale. This is partly due to the slowing down of the political opposition etc. However, the main reason is that the valuation of the public sector units is low. For example, the Airport centaur Hotel at Mumbai, which was bought from the government by Batra Hospitality for Rs. 83 crore. Early this year was resold to the Sahara Group for Rs. 115 crore six months later. Which works out to be a capital gain of Rs. 32 crore. This is more than the profits made by the Hotel during its entire life. Even the sale of shares in Blue chip public sector units like Indian Oil corporation, Bharat Petroleum Corporation and Hindustan Petroleum Corporation Ltd. (HPCL) were less than their actual value.

There are several issues that are responsible for the stop and start manner behind the disinvestment drive in India, not least opposition from the political organization and union fronts. In 1991, Singapore Airlines withdrew its bid for Air India, allegedly citing intense opposition from politicians, unions and Media. In cases where privatization has occurred, the benefits are not always obvious and in some instances have generated monopolies. This has in many instances provided fuel to those opposing privatization. The fierce standoff regarding the sale of majority stake in BALCO to private sector sterlite in 2001 highlighted the narrow self interest among political classes. The chief minister of the new state of Chattisgarh opposed the sale despite its attractiveness and the transparent manner in which it was handled. Such resistance could dampen enthusiasm for and jeopardize future disinvestments efforts. A political party that introduces some reforms could just as quickly oppose them when it is no longer in power.

In many instances, disinvestment has gone hand-in-hand with widespread corruption and insider dealings, particularly in cases of
privatization through asset sales and vouchers. The inadequacy of institutional and regulatory systems have contributed to a series of scams in the financial system including those in 1992 (Harshad Mehta) 1995-96 (IPO disasters) and 2001 (Ketan Mehta).

The backlash against disinvestments has been fuelled by the misuse of power by new owners of the privatized entities, their actions being driven by their own private interests at the expanse of the company. This issue recently surfaced following its acquisition of VSNL by Tata, the largest Indian group. Tata invested more than Rs. 1200 crore of surplus cash of VSNL in to its sister company Tata teleservices, the returns of which were considered uncertain. This move smacked of asset stripping and while it would be positive for Bombay House it was negative for VSNL.

There have been instances when the sale of the government’s stake in a public company to a private company has provided it with monopoly power. One recent example was the purchase of IPCL (Indian Petrochemical Corporation Ltd.) by Reliance, which led to an almost total monopoly in the petroleum industry.

Thus, there are several various issues that India faces in its disinvestment drive. Disinvestment is a complicated process. As India continues to privatize its public sector units, the government needs to pay particular attention to these areas of concern and strengthen its institutions to avoid pitfalls of disinvestments. The researcher highlighted some issues and propose future strategies and recommendations to tackle them.
6.2. Future Strategies Relating to Emerging Issues in the Disinvestment Process of Public Sector Enterprises in India

Disinvestment is an important policy initiative of the present government. Successive budget speeches of the finance minister had emphasized the resolve of the Government to privatize all non-strategic public sector enterprises (PSEs) and liquidate all chronically loss-making public sector units.

Following up on this policy, the Government had succeeded admirably in privatizing quite a few PSEs since 1999. However, of late, there appears to be considerable opposition not only on the modalities of disinvestment but against the very idea of privatization. Therefore, clarity is needed on some of these issues that are bothering policy makers.

What to Sell :-

One of the repeated objections relates to the wisdom of selling profitable units. At the outset, it is essential to clarify that privatization of only loss-making units is neither feasible nor desirable. Every effort has to be made to privatize all loss-making units, failing which they should be shut down after suitably compensating the workers. On this question, there can be no two opinions.

In the case of profit-making units, the question to be asked is whether they will continue to be profitable a few years hence when they will have to face competition without Government props such as purchase/price preference, subsidies and reservations. If the answer is in the affirmative, then these PSEs need not be privatized on economic grounds.
If the PSEs are of strategic importance to the economy, their control can remain in government hands. Privatization of profit-making PSEs can, however, be justified on ideological grounds, namely, that the governments has no business to be in business.

How to Sell:-

The second issue on which there appears to be considerable opposition is the modality of disinvestment. Now, this issue has assumed importance in view of the government’s likely loss of control over petroleum companies, following moves to privatize some of them. The concept of strategic sale has been opposed even though it is admitted that it will fetch more for the government. Those opposed to strategic sale have suggested that a portion of the government’s equity in these companies may be disinvested through an offer of shares in the capital market without relinquishing government control over management. This has obviously been suggested on ground’s of oil security. Such a method of disinvestments may help in broadening share ownership. However, unless there is change of management, there will not be much enthusiasm for the shares among the public. This method will also result in the government becoming the largest shareholder, though its shareholding may be less than 51%. This will take the enterprise out of the “Public Sector” and consequent accountability to parliament and other investigating agencies such as the central vigilance commission and the Central Bureau of Investigation while giving the government the power to indulge in back seat driving ! such an arrangement should be avoided at all costs as it endows power without accountability.
A strategic sale of companies engaged in retail selling of petroleum products cannot be considered 'Strategic by any means, especially as the oil and natural gas corporation and Indian Oil Corporation are still in government hands! The petroleum sector does not find a mention in the list of industries defined as 'Strategic by the government for the purpose of disinvestment.

Probably, all this talk of 'Oil Security' is nothing but a cloak to cover the real purpose, namely, to retain management control and consequent power of patronage. The disinvestment exercise has also thrown up other issues such as timing, valuation and transparency, shareholder agreements, monopolies, surplus labour and public support. Matter of concern and few but important points in this respect are as follows:

**Timing**

At present, there is an impression that there is unseemly haste in privatizing public sector units, especially the profit making ones. One would wonder whether the present time is right for disinvestment in PSEs in the hospitality sector.

In the past, government procedures did not allow it to realize opportunities of selling when the prices were favourable. This was the case in the GDR issues of VSNL and GAIL. At the same time, inordinate delay in disinvestment has a deleterious effect on the companies concerned. It not only precludes timely investment in the company, resulting in missed opportunities and profitability. It also saps the morale of the employees and gives a wrong signal to investors in the domestic and international community about the Government’s
Intentions. Hence, disinvestment, once announced should be completed within the shortest possible time and at the best price. Postponement should be only on the ground that the market situation is not favourable for obtaining a proper price.

Valuation and Transparency

An often repeated criticism heard is that Government holdings have been sold for a low price. Valuation arrived at by the Government is questioned and motives are attributed. It should be remembered that there is no such thing as a perfect valuation. Though most inputs that go in to valuation are objective, the ultimate judgement on the price is subjective, what is essential is that the reserve price arrived at by the time-tested methods of valuation should be kept secret and the highest bid above the reserve price should be accepted. A little more transparency in acceptance of bids should be preferable. For instance, the bids can be opened in the glare of TV Cameras and the highest bid announced to the bidding parties and the press. It is essential to generate confidence in the society that the government has secured the best price for its equity.

Shareholder Agreements

Before finalizing disinvestment deal, the shareholder agreement has to be clearly and carefully drafted to take care of interests of the Government and the purchaser. If this is not done, then the government may face problems such as the one relating to VSNL’s investment in Tata Teleservices from VSNL’s reserves. In this case, it was found that the shareholder’s agreement provided for consultation with the government in the case of Mergers or granting of loans but did not
mention anything on equity participation in other companies. Whether this was deliberate or somebody goofed up is anybody’s guess.

**Monopolies Issue**

It is essential that the disinvestment process should not result in the creation of monopolies. In the absence of adequate legal safeguards and a strong regulatory machinery, it will be difficult to ensure that consumers are not exploited by monopolies. For example, the requisite regulatory machinery is absent to prevent over exploitation of scarce natural resources for commercial gains.

Some have tried to explain away the governments decision to sell majority stakes in Indian Petrochemicals corporation to Reliance Industries by averring that it is not monopoly per se but abuse of monopoly that we should be bothered about. But, is there any regulatory machinery now that will decide what constitutes abuse of monopoly? Are there adequate laws to prevent such abuse? In the given circumstances in India, it will be referable to pre-qualify bidders for disinvestment from the monopolistic angle also. After all a government monopoly will be infinitely better than a private monopoly.

**Surplus Labour**

The next issue is what to do with surplus labour in PSEs that are being disinvested. Merely assuring employment for a period of one or two years after disinvestment is not a remedy. The headache of dealing with surplus labour is transferred to the strategic buyer along with the assets of the company. In a scenario where fresh investment is not forthcoming due to the adverse security climate, any attempt to retain labour for a certain period is likely to bring down the value of the
equity sold. The challenge is to minimize the ill effects of labour restructuring by providing adequate compensation, training/counselling for alternative jobs and the like.

Public Support

Ultimately, disinvestment will succeed or fail depending on the support the process gets from the public. It is easy to mislead the public by alleging that the priceless jewels of the country are being gifted away to unscrupulous businessmen. Unless the public understands the issue involved, their support for disinvestment will not be forthcoming. It was with this intention that the disinvestment commission had recommended the setting up of a disinvestment fund, into which all receipts from disinvestment would go and the monies would be spent on earmarked social sector projects such as housing, education and health. The public would then be convinced of the benefits of disinvestment.

So far, the government has not agreed to the creation of the disinvestment fund on the ground that prudent financial management precludes keeping of funds outside the consolidated fund of India. But it has agreed to set up a road fund into which receipts from levies on fuel would be deposited and the funds would be spent on development of roads. It is clear that unless urgent and radical measures aimed at reform are taken, most of the PSEs will be unable to overcome competition. It will be in the government's interest to remain in businesses that are highly profitable and contribute substantially to public interest and not fritter away its energies in running a host of Sundry, unprofitable businesses.
All such enterprises that are not of strategic importance will have to be disinvested urgently. And those that do not have to remain in the public sector and that cannot be disinvested must be liquidated without any delay. PSEs should not get any more financial assistance from the government in the form of equity, loans or grants. If they have worthwhile projects, they should approach financial institutions for assistance.

The time has come when the public sector has to be lean, efficient and capable of taking on domestic as well as international competition.

6.3. Suggestions And Recommendations for the effective Implementation of Disinvestment Programme in India

1. Fair, just and equitable procedure should be followed in carrying out disinvestment.

2. Lack of transparency and the decisions taken in hurry should be avoided.

3. Sale proceeds should not only be used to reduce fiscal deficit. They can also be used to finance National Renewal Fund. This fund can be utilized to take care of the workforce displaced as a result of disinvestment of public sector enterprises.

4. So far Government has focused on the Voluntary Retirement Schemes (VRS) that provides one time cash compensation. While providing unemployment compensation it is important to ensure that the unemployed do not fall in to the poverty trap. Focus should be given in creating alternative job in other segments of the economy. Government should also negotiate an agreement with the new owners concerning layoffs.
5. Strong domestic financial institutions and a well designed capital markets are necessary foundations for the success of privatization.

6. Economy should further be opened to private and foreign investors to increase competition. As it will give access to newer technology, increased scope for increasing export turnover and possibility of setting up third country operations.

7. The government should also strengthen its corporate governance institutions to ensure that privatized entities are not abused by their new owners through asset stripping.

8. Few changes should be done in the architecture of the corporate sector. There also needs to be a sound Internal Audit System and clear guidelines regarding intra-company transactions.

9. The dilution of the stake of the government should be carefully analyzed. The dilution which leads to transfer of management in areas of strategic importance should be avoided.

10. The policy of Navratna should be encouraged.

11. Disinvestment must be done on realistic basis. There must be a proper evaluation not only from the commissions point of view but also from the market point of view. For this eminent economists must be involved and professional appraisers should be used.
12. Targets should not be fixed as it leads to distress selling in order to meet the target.

13. A more comprehensive disinvestment policy should be announced by the authorities that defines a list of enterprises eligible for disinvestment, sets a guideline for their sales to the private sector and establishes a mechanism for disinvestment.

14. The authorities should establish a regulatory framework prior to the disinvestment of natural monopoly enterprises and deregulate industries to encourage competition.

15. Labour Retrenchment programme should be implemented to compensate workers who lose their jobs due to shutdown of non-viable enterprises.

16. Government should neither extend special privileges nor impose extraordinary conditions for the operation of disinvested companies.

17. Disinvestment process should be given maximum publicity and the enterprises should be sold through auction openly.

18. The authorities should ensure equal access to information for all potential investors. The disinvestment programme in the non reserved sector should be opened to foreign investors to attract continued overseas interest in the development of the Indian economy.

19. Rising uncertainty and delays in the disinvestment process due to opposition from various parties should be avoided as it
causes a low realization and a reduced foreign interest in Indian disinvestment.

20. Government should initiate efforts to evaluate unprofitable enterprises and consider their sales. The sale proceeds of these enterprises should be deposited in to a bank, as it will give better revenue gains instead of suffering losses with its continuation.

21. Authorities should give special consideration for restructuring and rehabilitation of vulnerable public sector enterprises.

22. Adequate legal safeguards and a strong regulatory machinery should be adopted to avoid monopolies issue. It will be preferable to pre-qualify bidders for disinvestment from the monopolistic angle also.

23. A long term policy for training and educating the large work force in technical and managerial aspects, software design and maintenance and service development should be an integral part of any future telecom policy.

24. Decision making committees must consist of professional from a wide range of fields to strengthen the analytical component of any policy design and implementation.

25. In the context of the changing business scenario, policy regarding marketing, usage and ownership of data com channels and other telecom services needs to be amended.

Thus, disinvestment of public sector enterprises is need of the hour. As it will encourage such public enterprises to work in a
competitive environment, thereby making their management more responsive towards the customers need and changing technology and raising their working efficiency and also the rising demands of their investors will make them more accountable too and the resultant rise in their revenues will be a good fruit. Beside this, selling of these white elephants on which crores of rupees have been wasted will give a large one time capital gain, which itself can be a panacea for a debt ridden country like India suffering from overload of nationalization.

Last but not the least disinvestment can be regarded as a sound economic policy, a good social strategy and a prudent political philosophy. But transparency is vital for a successful disinvestments programme to bring credibility in any deal.