CONCLUSION

The foregoing analysis in this chapter reveals that prices for the steel products determined by the Government operate to hamper the growth of the steel industry. It has produced a number of negative phenomena. For instance, the retention prices received by the producers were substantially below the controlled sales prices until 1973-74. The Government's unwillingness to allow sufficient increases in the retention price actually discouraged greater production of tested steel.

Another distortion of the pricing system adopted by the Government in the case of iron and steel industry is that it does not provide for cost reduction. In fact, it encourages cost inflation which consists in the provision of depreciation, tax rebates for development and retained profits which are deployed for expansion of capital base which is used for the computation of the retention prices. Higher becomes the capital base, higher up are the prices adjusted to allow the guaranteed return on this enlarged capital base. The sticky prices and the rigid cost pattern during slack period reduce the level of output and push the unit cost of production. The effect of this policy is also to make the production of
less costly and substandard alternatives, such as untested steel, more remunerative to the producers. For this reason, the Government's pricing policy for the steel industry encouraged the substitution of inferior for the superior quality of steel products.

The most serious defect of steel price control and pricing system was the distortion of both retention and selling prices relative to the prices of other commodities and the cost of producing steel in India. The spiralling cost of production and low retention prices yielded low return on capital per ton of saleable steel, viz., 0.005 per cent in the case of Bhilai, the marginal producer, in 1973-74. It also has definite implications on the quality of products rolled and economic efficiency of the undertakings.

Although operating costs were as a rule fully covered by retention prices, overheads were not. The estimate of a standard block capital per ton of saleable steel in 1962 was derived from the actual purchase costs of TISCO's plant and equipment, which were mostly installed before or immediately after World War II, and were in no way related to replacement costs.

These measures of capital block were particularly untenable as bases for the computation of return to the
the public sector steel plants. The public sector mills had difficulty meeting operating costs from their retention prices and had to borrow from the banks to cover their deficits. It would have been impossible for them to earn an adequate return on their investment so long as they received prices based on the out-of-date capital costs of the private sector plants. To give a forward-looking price structure to the steel plants and also to provide incentive for cost 'minimization' in the public sector steel plants, it is recommended that the principle of 'marginal cost pricing' be substituted for the cost-plus formula.
CHAPTER VII

CONCLUSIONS

The thesis concerns itself with a critical examination as to how far the aspirations of 'Democratic Socialism' have been achieved; whether the maximum good of the maximum number has been the result of the working of public enterprises or they have failed to achieve the desired results.

The analysis in Chapter I demonstrates that public sector in India is wedded to 'Democratic Socialism' which promises to lift the economy from lower level to a higher level of equilibrium and improve the living standard of the populace. The private sector by and large is not interested in providing these social and economic overheads although they are becoming conscious of their social responsibilities. Hence, the onus is on the Government to provide through public enterprises right type of goods and services which would ensure accelerated economic development of the country. This being the goal, the State has made massive investment totalling Rs.11,097 crores till the end of 1975-76 in the public enterprises.
To step up the growth rate further, it is also essential that the capital is accumulated at every convenient point of activity. The public enterprises should not lag behind the rest of the economy in capital formation. In fact 'surplus' from public enterprises would constitute savings for productive investment on the one hand and contribution to the national social welfare programmes on the other. 'Surplus' is also necessary for public enterprises to self-finance their expansion, improvement and modernisation and for providing further employment opportunities in the country.

Chapter II critically evaluates in the light of the above avowed aims of the public enterprises the working results during the period 1965-66 and 1973-74. The study reveals that public enterprises have yet to be an effective means of resource-generation. This contention is supported by the low profits and large deficits. For instance, of the whole decade under review, public enterprises made a notional profit of Rs.75 crore which yielded a return of less than 2 per cent only in 1973-74. Of the 95 running concerns, sixty-two enterprises had declared dividend on equity which was as low as "less than 1 per cent". The aggregate capital of these enterprises amounted to 77
per cent of the total equity. Assuming that if high dividends were not declared, high profit-ploughbacks would amount to resource-mobilisation, it is noted that average rate of return was 1.68 per cent, which was far less than the 'opportunity cost' of the capital invested. It can, therefore, be safely concluded that the performance of public enterprises remained highly unsatisfactory.

Contrary is true to say that they have acted as a drain on the national exchequer due to heavy deficits which worked out at 14 per cent of the equity at the end of 1973-74. This, in the ultimate analysis, has to be made good by the Government unless future operations of these enterprises become compensatorily profitable. The hard pressed case of cumulative deficits is the Engineering Industry of the public sector whose cumulative deficits amounted to Rs.231.21 crore or 21 per cent of the total capital invested. It does not mean that other public enterprises are not "in the red". All the public enterprises, excluding Petroleum, Trading and Marketing, have accumulated very large deficits over the period of their operations under review. Besides, loss of income to the Government is also implicit in equity-device of capitalisation to the extent of cost of capital whenever an enterprise does
not earn profits enough to pay a dividend on equity. For instance, in the solitary year of profit, viz., 1973-74, eight enterprises with an aggregate capital of Rs.98.95 crore, which did not declare dividend, entailed loss of Rs.5.9 crore, if this was computed at the minimum 6 per cent rate of interest. The cost of capital or 'opportunity cost' may be regarded as an 'unnoticed recurrent loss' of income because this does not enter the books of accounts. It may be said that the 'explicit' and 'implicit' losses amount to a very high proportion of the capital over the period of their operations.

In Chapter III, inquiry into the factors causing deficits revealed that cost of production in public enterprises was excessive due to, in the first instance, large idle capacity. For example, in 1972-73, out of 35 units analysed, it was found that in 14 enterprises utilisation of capacity was above 75 per cent; in the case of 12 units it was above 50 per cent; in the case of 6 it was less than 50 per cent, and three could utilise even less than 25 per cent. Idle capacity on such a large scale is attributable primarily to long period of gestation in capital-intensive projects. Hindustan Electricals (India) Ltd. furnishes an example which was incorporated on 29 August, 1955. The project
report, as accepted by the Government, had anticipated eight years to achieve full production in the factory. The eight years were a period of abnormally high under-utilisation of capacity. Teething problems, including technological difficulties and initial bottlenecks, also acted as constraints which militated against full utilisation of capacity in a number of cases. For instance, fertilizer plants of Neyveli Lignite Corporation which were commissioned in 1965 had to work to low capacity until 1969 due to technological difficulties and initial bottlenecks.

In addition to these, there are evidences to suggest that, on balance, investment planning at the very beginning did not take into account demand for the product. For instance, Government entered into an agreement with the Government of USSR on 29 May, 1959, to establish in the public sector plants for the manufacture of antibiotics, synthetic drugs, surgical instruments, phyto-chemicals and glandular products though demand for those products did not justify establishment of these units. As a consequence, the level of production, in the first two years, in surgical instruments' plant was about 19 per cent of its capacity. In 1972-73, it was 24 per cent, and in subsequent years also the level of production did not rise much. In antibiotics
plant at Rishikesh, the production of commissioned products was 48 per cent in 1975-76. Such instances support the contention that demand was not adequately assessed for the products at the time of initial capital investment.

Likewise, lack of coordinated market research and development programmes is yet another factor contributing to low utilisation of capacity. For example, Indian Drugs and Pharmaceuticals Ltd. (IDPL) can increase demand for its products by producing consumer-end products, following the suit of the international companies like Bayer, Parke-Davis, Sandoz, Glaxo, etc., which manufacture products extending from cosmetics to electronics, veterinary products, pharmaceuticals, dye-stuffs, laboratory chemicals, industrial raw-materials and intermediate, textile chemicals, agro-chemicals, baby-food, tooth-pastes, shaving creams, etc.

Unrealistic production targets also account for idle capacity in the public enterprises. Management used to fix easily accessible targets to cover up their inefficiency. It is essential that annual targets of production are laid down after taking into account all the relevant factors, including rated capacity and the size of demand which must be assessed by the enterprise through market surveys. It calls for a system of
'checks and balances' in production planning to avoid low targets of production.

Yet another cause of low utilisation of capacity is the strained industrial relations. To illustrate the point, public steel mills alone lost 20.96 lakh manhours during 1967-68 and 1970-71, entailing financial losses of Rs. 986.45 lakh.

Poor maintenance of equipments and machinery also brought in its trail loss of production. For example, destruction of equipment at Rourkela at one time necessitated some stripping of parts from one unit of a mill to replace parts in another. Whereas public sector steel plants could not operate efficiently, other public enterprises bore excessive costs of unnecessarily large accumulation of inventories. For instance, inventories of public enterprises increased from Rs. 361 crore in 1965-66 to Rs. 2,485 crore in 1973-74. If public enterprises could reduce inventories to 2 months' output, substantial funds would have been available for gainful employment in the undertakings.

It is worth considering that cost pattern of public enterprises is also influenced by 'social interests' comprising surplus labour, excessive cost
of wage-and-non-wage benefits, provision of more consumer-amenities than a private enterprise.

Overstaffing is a common feature of almost every public enterprise. For instance, the public sector steel plants were to hire between 6,000 and 8,000 persons. The actual work force of these enterprises is now double the original estimates. Relative disregard for cost minimisation has encouraged the hiring of additional workers to obtain marginal increments in output.

Bane of overstaffing is seen in the form of absenteeism and indiscipline. To illustrate, the Aircraft Factory and the Engine Factory of the Hindustan Aeronautics Ltd. lost 20.41 per cent and 21.18 per cent of mandays respectively due to absenteeism in 1966-67. It is significant to note that while there is surplus labour, there are instances of overtime payments to the staff. For example, Fertilizer Corporation of India, despite surplus labour, paid by way of overtime allowances Rs.16.02 lakh in 1966-67. It illustrates waste of scarce resources by public enterprises.

Higher cost of production is also traceable to excessive spendings on wage-and-non-wage benefits to
employees of the public enterprises. The successive five year plans emphasised the responsibilities of the public enterprises with regard to labour. Explaining the implications of this approach, the Third Five Year Plan pointed out that the economic activity was not to be conceived of only in terms of output and returns; the principal test of this would be the good of all those who were engaged in it. There is, however, a strong need to follow a balanced approach in incurring expenditure on productive and non-productive activities. They should have relationship with productivity which is not taken into consideration at present. To ask the public enterprises to be 'model employers' on the basis of higher wage-and-non-wage benefits would be a misnomer, if their productivity and profits are not increased. To compare the working of public enterprises on the basis of this norm with the private enterprises, the latter are better 'model employers' who pay higher wages and more non-wage benefits to their employees. Public enterprises are over-burdened with financial cost of these benefits. For instance, during 1965-66 and 1969-70 rate of increase in expenditure was 16.29 per cent as against 1.30 per cent of increase in labour productivity. For the whole period 1965-66 to 1975-76, compound rate of increase in expenditure per employee was 17.1 per cent as against 1.15 per cent for
labour productivity. Wherever the enhancement in expenditure on employees of the public enterprises is not linked with productivity, a case emerges, as if a self-evident one, of inflated cost of production. I, therefore, recommend that the welfare expenditure of public enterprises must be decided on business economics rather than on social grounds.

Similarly, public enterprises carry the burden of townships. The total gross capital expenditure on townships accounted for Rs. 406.9 crore out of the total gross fixed assets of Rs. 11,451.2 crore in 1976-77. Thus, the expenditure on townships constituted 3.6 per cent of the total gross investment in fixed assets. Rate of return on total capital invested in 1976-77 was 3.6 per cent. If the township outlays were excluded, it would have increased to 5.2 per cent. If township burden is removed, it would thus have a favourable impact on the return.

The other way in which a public enterprise bears social cost is by providing certain of its outputs to consumers and regions that do not pay the related costs in full. Such operations of public enterprises are marked by excessive costs which their counterparts in the
private sector do not usually have to provide for. The argument is not that such operations should be given up, but that the expenditures incurred, being merged in the general costs of the enterprise, inflate the overall cost pattern to the disadvantage of the other consumers.

Additionally, our public enterprises are also under the stress of having to incur expenditure to satisfy the rules of 'public accountability' which take the shape of investigations by Committee on Public Undertakings, criticism by the members of Parliament, audit by the Comptroller and Auditor-General and public criticism in the press. The public enterprises are impelled to conduct their operations, especially the expenditure operations, in such a way that all the relevant rules are satisfied and there is nothing 'irregular' about any transaction. The procedure built up for the sake of 'public accountability' involves, as one of the important consequences, delays in decision-making. This has two defects: firstly, certain possible economies may be lost due to impromptitude of the decision; and secondly, a decisional framework characterised by delay dissuades the managers in the long run from evincing positive interest in prompt action. It is interesting to note that Professor J.K. Galbraith has stressed the
importance of timeliness in preference to precision in business decisions.

It would also be necessary to organise public relations and publicity work to achieve the objective of keeping the public adequately informed and to secure acceptance of public enterprise policies, more so because no statutory requirements regarding consumers' consultative councils exist for these enterprises.

On the basis of the foregoing analysis, the conclusion is drawn that the cost pattern of our public enterprises is excessive due to idle capacity, deficiencies in investment techniques, production planning, inventory control, marketing management and planning of manpower. Stress on the public enterprises to act as 'model employer' and fulfil the needs of 'public accountability' has added to the cost of production. In my opinion, 'social obligations' must also be wedded to productivity and profitability. Similarly, Parliamentary control which envisages public accountability should be exercised with due care. The procedure should be such as to maintain autonomy of the public enterprises and help the decision-making process. If bright image of public enterprises is to be projected and if they are not to suffer due to lack of consumers' consultative councils, endeavours must be made to organise public
relations and publicity work. In the ultimate analysis, if the public enterprises are to be worthy of public confidence, they should make continuous efforts to serve the good of the public in an efficient manner.

Nevertheless, excessive cost and low returns are the manifestations of unscientific organisation and inefficient bureaucratic management. Analysis in the Chapter IV discloses the fact that these enterprises bear the cost of organisation which is inefficient at various levels of management, such as delays in decision-making and consequent operational inefficiency. Professor Q.H. Farooque's comments in this respect are quite revealing, "These enterprises, in spite of the best Government care and attention, have failed to inspire the team-work. What is to say of giving lead to the private sector as regards sound management, they do not even approximate the conditions obtaining in the enlightened private industrial concerns."\(^1\) It is sufficient indication that managerial efficiency of public enterprises is at its low ebb. Hence, there is a good scope for reduction of costs through improvement in managerial efficiency and application of business principles in them.

Close examination of the working of the public

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1. See the text of the Chapter IV.
enterprises revealed that the existing management has tended to be over-centralised in the hands of bureaucrats who are reluctant to decentralise functions even though justified by economic expediencies. Such practices have led to delays in decisions and operations.

From the analyses in the Chapters I to IV have emerged four questions of significance in relation to pricing system in our public enterprises which have been fully investigated in the Chapters V and VI, viz:

(a) have the objectives been specified to harmonize economic and social interests which the public enterprises are called upon to fulfil and the norms to measure efficiency;

(b) is there a consistent pricing policy;

(c) does there obtain 'minimum cost level' viz-a-viz pricing; and

(d) does there exist a system of sufficient consultation with the management to fix prices including profit or 'surplus' targets to provide incentives to management?

Findings of the analyses in the Chapters V and VI support the view that there is need for separation of non-commercial activities of a public enterprise from
economic ones to avoid confusion. The management, at present, in most cases, does not fulfill financial obligations. If objectives are specified for individual public concerns either on the basis of product, customer, market or zone, there will emerge accordingly a policy of 'subsidy' for losses sustained by public enterprises under different sets of circumstances. Losses resulting from "administered prices" or those resulting from "inadequate project planning" and "constructional delays" must be subsidized. However, the present practice of using "Depreciation Fund" for wiping out losses is not a desirable practice because it eventually undermines the financial soundness of these enterprises as a commercial entity.

It is significant to note that objectives have to be determined for the disposition of 'surplus' to harmonize the economic and social interests. In this context, it is worth considering that, first, the pattern of distribution of 'surplus' must be laid down in advance; secondly, the pattern must be flexible enough to meet the requirements of national economy as a whole; and, finally, major portion of the surplus must be earmarked for general capital formation.

Investigation into the pricing techniques in public enterprises revealed that Government exercises
rigid control on the prices of public enterprises. It must, however, be cited that price controls hampered the growth of the iron and steel industry. It produced a number of negative phenomena ranging from deterioration in the quality of steel products to the fall in steel production. The sticky prices and the spiralling cost of production tended to reduce the level of output on the one hand and discourage production of superior category of steel due to unremunerative prices on the other. The most serious defect of steel price control was the distortion of both retention and selling prices relative to the prices of 'other commodities' and the cost of producing steel in India. The high cost of production and the low prices caused low return on capital block per ton of salable steel. Thus, it has definite implications on the quality of products rolled and operational efficiency of the public steel mills. It is impossible for the public enterprises to earn an adequate return on their investment so long as they are the catchers of unrealistic prices.

When prices are determined, there must obtain a 'minimum level of cost' viz-a-viz prices for the products of our public enterprises. The findings of this enquiry indicate that the prices became untenable
to our public enterprises because they were not sufficient to cover the costs of production. In the case of Iron and steel industry, for example, the rate of growth of prices was lower than the costs. During the period 1961-62 and 1969-70 the annual rate of growth of prices for steel products was 8 per cent as compared to 10 per cent for the cost of producing steel in the country. It demonstrates that there does not exist a pricing system consistent with the level of costs in our public enterprises.

It is, therefore, imperative to constitute a competent body to help the government evolve a consistent pricing policy for our public enterprises. To avoid the conflict between the maximum 'economic' and 'social' returns, it would be worthwhile to apply the principle of 'marginal costing' in these enterprises.

It can be pointed out without any fear of contradiction that prices based on 'cost plus' formula are not conducive to reductions in the costs. The cost must be reduced to a minimum level for the determination of prices by eliminating factors causing escalation in the costs, e.g., large idle capacity, deficiencies in project planning, constructional delays, inadequate production management, heavy inventories, lack of proper marketing management, large overheads, surplus labour force, low productivity of labour and capital.
There are, in fact, manifestations of managerial inefficiency due to organisational deficiencies and lack of initiative on the part of management.

The main conclusion of this study is that, to ensure success of the public enterprises, it is necessary to run these enterprises on sound principles of business management. The decision-making process must be rationalised so that decisions are taken promptly at all levels of management, i.e., board of directors and down to the lowest level of management. The public enterprises which have become adjuncts to the ministry concerned due to official hold on their boards must be given a board which must be diversified, consisting of members drawn from diverse fields, e.g., education, research, industry, commerce, banking, etc. These organisational reforms are compatible with 'operational autonomy' of public enterprises and 'public accountability', divorced from political considerations and arbitrariness.

The analytical study significantly reveals that, in the present set-up, there is conspicuous absence of norms to measure the managerial efficiency of our public enterprises. 'Money profits' must not be taken as a true yardstick, except where competitive conditions prevail. Efficiency must be measured in relation to
certain objectives, viz., economical use of capital resources and other inputs, savings on overheads and inventories, higher productivity of labour and capital, changes in unit cost of production of a given quality. These criteria have not been made use of in our public enterprises. If implemented properly, these measures would go a long way in enhancing the profitability of our public sector enterprises.

It is significant to note that the 'Surplus margin' is fixed too generally and without sufficient consultation with the management who alone can say what is feasible and what is unfeasible under a given set of conditions. An 'overall' surplus target for the public sector as a whole is not very meaningful from the angle of improving 'operational efficiency' and providing incentives to management. 'Surplus' targets should be, therefore, determined for individual concerns in close consultation with the management, after taking into consideration the supply and demand conditions, and impact on the private sector viz-a-viz the national economy as a whole.

On the basis of the findings of this study, it can be asserted that, surplus being the primary objective for social welfare programme, pricing policy
must be so formulated as to help the public enterprises strengthen their marketing and technological position, provide the community with products and services competitive in price and quality, bring about higher productivity and assist in 'general' capital formation. To attain these objectives, Government must pay full attention to the concept of 'marginal cost pricing' to substitute for the arbitrary methods of fixing prices on the basis of 'cost plus' formula. This is essential for the fulfilment of the social responsibilities of management and their trusteeship towards citizens of the country.