CHAPTER V
TOWARDS PUBLIC SECTOR AND NATIONALISATION

Indian economic planning, as stated explicitly in the Five Year Plans, is aimed at creating a Socialist State. This has meant encouraging public as against private investment in industry. The objective of the economic policy which India has followed since independence can be summarised as follows:-

a) rapid economic growth through planning, and a
b) more equitable distribution of income and wealth.

These objectives are inter-related and the main policy instruments used to achieve these objectives centre around economic planning; land reforms; wealth distribution; nationalisation; income distribution and taxation.

In the years immediately after independence, there seemed to be a growing acceptance of the public corporation as the appropriate form of organization for public enterprise. The growth of Indian public enterprises or public corporations can be directly related to various industrial policy resolutions of the Indian Congress Party. The Industrial Policy Resolution of 1948 envisaged that, "management of State enterprises will, as a general rule, be through the medium of public corporation." 1

In fact, the evolution of the public sector in the economy and polity of India is of recent origin and can be compressed within the period following independence. Prior to

* State here means the Central Government.

1947, there was virtually no public sector in the Indian economy. The only instances worthy of mention were the Railways; the Posts and Telegraphs Department; the Port Trusts and the Ordnance and Aircraft factories. The Industrial Policy Statement (Resolution) of April 1948 is indeed significant as it enunciated the respective roles of State and private enterprise and helped to bring the public sector into limelight. It indicated that: "a dynamic national policy must be directed to a continuous increase in production by all possible means, side by side with measures to secure its equitable distribution. The problem of State participation in industry and the condition in which private enterprise should be allowed to operate must be judged in this context."  

The industrial field was accordingly divided into three groups:

a) Strategic industries which should be the exclusive monopoly of the state e.g. manufacture of arms and ammunitions, the production and control of atomic energy and the ownership and management of the railways and transport etc.

b) Key industries like coal, iron and steel, aircraft manufacturing, ship building, mineral oils etc. Where existing private concerns would be allowed to operate for the next ten years, subject to the stipulation that the establishment of new undertakings in this field would be the

responsibility of the State.

c) Remaining industries where private enterprise would be allowed to operate subject to Government control and regulations.

While the Government was trying to achieve economic independence, it was encouraging foreign private investment in fields where India was lacking in technology, capital or trained personnel. Economic independence has been defined as a situation in which national institutions have the right, capacity and power to take and implement decisions affecting the national economy and development and its component units without a de jure or de facto veto power being held by foreign individuals, enterprises, interest groups or Governments. In fact, this sort of economic development seeking to achieve economic independence was more explicitly equated with State enterprises.

However, as the Government began to move into mining and manufactures, misgivings began to be felt about whether the public corporation was the most suitable organizational form. So the Planning Commission Report on the Efficient Conduct of State Enterprises recommended that the general principle regarding choice of form should be that where the nature of work is substantially commercial, the joint stock company was preferable but in all other cases the public corporation was desirable, especially for undertaking extension of the functions of the Government, such as broadcasting, transport and irrigation.

The next landmark in the emergence of the public sector in India came with the Industrial Policy Resolution of April 30, 1956 passed basically to prevent private monopoly and the concentration of economic power in the hands of small numbers of individuals. This Resolution stressed that a large and growing public sector was essential in order to achieve the socialist ideal and for rapid development. The Industrial Policy Resolution of 1956, which wanted to speed up industrialization compelled the State to assume a predominant and direct responsibility for setting up new industrial undertakings, for only the State could provide those that are essential and that require investment on a large scale. Private enterprise usually shied away from long-term investments and sought short-term goals and quick profits. An attempt was therefore made, to ensure full contribution by both, the public and private sectors as complementary aspects of the same effort. The striking feature of both these Resolutions is their pragmatic character and absence of purely doctrinaire considerations. The Resolution of 1956 envisaged that the public enterprises will not only augment the revenue of the State but also provide resources for further development in fresh fields. Therefore, for such a realization it was considered essential that all industries of basic and strategic importance or in the nature of public utility services, should be in the public sector.

The three categories of industries were reclassified.

Mineral Oils came into the first category of industries, the further development of which would be the exclusive responsibility of the State. In fact since 1948, progress in the public sector has been very rapid as is evident from the number of enterprises that have been initiated in the public sector ever since 1947 and as indicated below:

a) defence and strategic establishments i.e. Hindustan Aircraft Ltd, Bharat Electronics.

b) public utility undertakings, like the Indian Railways; Air Transport Services and Telephone Industries.

c) Industries, such as Sindri Fertilizers, Indian Refineries Ltd, (now Indian Oil Corporation); Hindustan Steel Ltd.

d) Shipping and

e) Other projects like Damodar Valley Corporation, State Trading Corporation and many more.

The year 1956 also marked the enactment of the Indian Companies Act of 1956 under which are incorporated all companies which have been set up in the public sector. The evolution of the Act is instructive in showing the Government's growing resolve to control the private sector. The role of the public sector began to expand. Raw materials fell mainly in the sphere of public sector, production in the mixed sector and marketing continued primarily in the private sector. Thus, the Indian economy which started out after independence, oriented predominantly towards
private enterprise has since been assigning to public enterprises an increasingly significant role. In fact, in a centrally planned economy like that of India, it was considered that public enterprise could be operated on the basis of maximum profits so as to become the source of finance for further economic development.

Pandit Jawaharlal Nehru, the first Prime Minister of India had conceived of a mixed economy for the future of India with both the public and private sectors, but with effective control of the latter by the Government in the national interest. While the public sector must obviously grow, both absolutely and relatively, the private sector, as we have stated in the Industrial Policy Resolution, will be given a fairly wide field subject to the limitations that are laid down. Pandit Nehru declared that he did not consider it worth while acquiring existing private units; he wanted them to contribute their best to the national wealth. But, in this scheme of things, the control by foreign parties in the industrial sector had to be slowly but definitely eroded. 6

It would be relevant here to go into the pros and cons of a public enterprise and the aims and objectives of the Government in favour of the public vis a vis the private sector. The usual organisation of a public sector is that of a limited company with the Government holding the whole or a majority of shares.

A public sector unit is wholly owned by the Government and is generally created by or under a special law defining its objectives, powers and privileges, duties and immunities. As a body corporate, it is a separate entity for legal purposes and can sue and be sued, enter into contracts and acquire property in its own name. Except for appropriations to provide capital or to cover losses, it is usually independently financed, obtaining its funds by borrowing either from the Treasury or from the public, and through revenues derived from the sale of goods. It is generally exempted from most of the regulatory and prohibitory laws and procedures applicable to the expenditure of public funds. In most cases, employees of public corporations are not public servants and are recruited and compensated under terms and conditions which the corporation itself determines.7

All these impart to the public corporation a high degree of operating and financial flexibility. Most of the companies in the public sector in India are wholly Government-owned. A few however, have a small sprinkling of private shareholders.

The term public enterprise for a public corporation is used to denote those services provided by the Government which provide essential services for "civilized life".8 What was novel was the extension of public control and management to basic supply and service industries by means of the newer form of organization which students of public administration have called the "public corporation" and which grew in response to particular

circumstances and was not an invention of political scientists. In India, public enterprises have been set up as instruments of national economic policy and economic levers with which planning objectives are to be realized. Effective planning of the national economy can only be achieved if the planners can control the resources. The best control comes with ownership so that the amenability of publicly owned industries and services is essential for the success of the planners' proposals. Public corporations generally run industries which provide services to individual customers. And the consumer's needs are compounded of two elements relating to efficient and adequate service to be made available at an economic price.

Government decisions to introduce public enterprise have been made for various reasons based on the Government's resolve for the promotion of domestic private enterprise; the need for heavy initial investment of funds and other resources beyond the capacity of the private enterprise; the achievement of development goals outside the interest of private enterprise; the production of greater Government revenue and Government control over foreign business and investments. No wonder, joint ventures were encouraged by the Government so that the State could gradually gain greater control over existing foreign private investments in due course of time.

The dual objective of a public enterprise is the promotion of economic growth and financial aims, such as generating a surplus and earning foreign exchange. On the other hand are the social or more general aims like reducing unemployment,

regional disparities, poverty, improving the quality of working conditions, protecting consumers from arbitrarily high prices of goods and services, improving the quality and range of goods and services, helping to transform the economic structure, conducting its affairs in harmony and conformity with national economic plans and targets, and acting in the national interest. But the overall aim of the public sector is to produce a financial surplus. A continued deficit cannot be explained away in terms of compelling social aims.

As a result of deliberate Government policy, there has been a tremendous growth of public enterprises in India. The diverse areas of activity in which public enterprises have been constituted by India include the traditional public utilities; fuel and power; communications; development of river basins; new towns and specified backward areas; finance; manufacture and commerce. Public enterprise, generally confined to a few basic industries in the developing economics is expected to sell its products and services at low prices, leaving profitable markets to the small businesses. Thus, the public corporations have manifested themselves in a wide range of fields of economic activities. Therefore, public ownership has been strongly advocated as an essential means to further economic progress.

Public enterprises are normally used to stimulate private enterprise, directly or indirectly; to displace private enterprise either through nationalization of specific private enterprises or through the pre-emption of certain sectors of economy as the exclusive domain of public enterprises; to supple-
ment private enterprise by filling gaps left open by private enterprise and to participate with private enterprise in undertaking joint ventures.

Joint ventures, where the private party happens to be a foreign company, though advantageous to both the host country and the foreign company may pose a difficult problem of control arising out of a clash between the developmental concerns of the host Government and the profit-maximisation motives of the foreign partner. Certainly, public enterprises are organs for achieving goals of economic and social development and therefore it would be true to say that private enterprises cannot completely ignore social purposes and public enterprises, equally, cannot completely ignore considerations of profit.

It is for this reason that private and public enterprises cannot be divided into two watertight compartments. Though distinct from each other, they do share a lot in common: management of personnel, labour relations, cost-efficiency, internal organization, delegation of authority, price control, and profit factor.

A specific and important role has been marked out in India for the public undertakings of a "core sector", but it seems even more important that the public sector build up infrastructure for the private sector - otherwise it would not be possible to attain the "commanding heights" of the economy, as the picturesque phrase coined by Aneurin Bevan that has been adopted by the Indian planners suggests. The World Bank Mission which

toured India in 1960 recorded that the issue of public versus private enterprise has lost some of its sharpness because it has become more widely recognised that both sectors of the economy have their contribution to make. In addition, public enterprises can be used to accelerate technological progress and fuller utilization of capacity. A large public sector can improve the composition of investment, because a larger proportion of the total investment remains under the control of the Government. In fact, a powerful motive for nationalization was the desire to secure local economic control and ownership. But ownership means little if the countries remain technologically dependent. Technological dependence may take the form of foreign financed investment, using foreign managers; of joint ventures with some foreign managers and finance; and of local ownership with contracts to secure foreign technology. The public sector was set up to ensure that the ownership remains in the Indian hands and only foreign technology is obtained on mutually advantageous terms. The leaders in the developing countries tend to see the linkage of the national economy to foreign-owned enterprises as a betrayal of the national interests. Others see such links as opportunities for national growth, provided the links are properly managed and carefully exploited. A large and growing public sector increases the amenability of the national economy to effective development planning.

The public enterprises strive to protect consumers from monopolistic exploitation. Therefore, nationalization provides one of the means the State can employ to protect the consumer against excessive prices and to safeguard against undesirable concentration of private economic power. It contributes towards better co-ordination of marketing aspects.

Some public enterprises are set up principally to protect or create employment. One common sequence is for a private concern to run into financial difficulties and for the State to take it over to protect the jobs that would be lost if it were to close down. Some public corporations help in the growth of ancillary industries. This is particularly true in the case of the petroleum industry.

The public corporation (statutory corporation) has been hailed as the most important invention of the twentieth century in the sphere of Governmental institutions. Public corporations have indeed arisen as an empirical response to organizational needs. The public corporation form attempts to strike a balance between autonomy and control. It is clothed with the power of the Government but possessed of the initiative, flexibility and willingness to experiment that characterize a private commercial enterprise. It seeks to secure freedom from parliamentary supervision over day-to-day management and from treasury control over personnel and finance for industrial or commercial
undertakings. The public corporation is designed to eliminate delays, red tape and excessive regard for precedents.

This, of course, indicates the ideal. The actual Indian experiment initially proved different in respect of certain public enterprises because they did not enjoy independence from the executive and so functioned virtually like Government Departments. The Estimates Committee Report of 1953-54 found that the Government Companies in India are, 'more or less extensions of Departments and are run almost on the same pattern, with minor changes here and there. Many times the day-to-day business tends to be transacted between the Managing Director and the Ministry.'

Motives and objectives for the creation of public enterprise in India have been clarified in the Plan documents. The objects of the First Five Year Plan were to correct the disequilibrium caused by war and partition, and to initiate a process of all-round balanced development which would both ensure a rising national income and set in motion the process of structural alteration in the Indian economy. A comprehensive investment programme was drawn up and specific production targets were fixed for various sectors. But due to financial constraints the public sector was unable to fully execute the investment programme with which it was charged. Therefore, licences were issued to the private sector in areas which were reserved for public sector expansion. These included coal, oil,

13. Ibid., p.63.
fertilizers among others. Three Western Oil Companies were permitted to establish refineries. The Government signed a deal with STANVAC (later Esso) for oil exploration with minority participation by the Indian Government.

Nevertheless, the Second Plan document stressed the importance of using the public sector as an instrument for preventing concentration of economic power. The Third Plan document reiterated this, stating that rapid expansion of the public sector was to serve a twofold purpose. It would help to remove certain basic deficiencies in the economic structure while at the same time it would reduce the scope for accumulation of wealth in private hands. In addition, it would speed up the growth of economy as a whole.

Yet, the Government was not ready for a large scale programme of nationalisation and was looking more favourably towards the private enterprise. Ministers stated categorically that there is no intention of nationalizing either the banks or general insurance. Sardar Patel, then Deputy Prime Minister, echoed with characteristic brevity, "Take it from me that this Government has not got the capacity and means to undertake nationalization of any industry at present. "You should yourself realise that industry is to be established before it can be nationalised. India is yet industrially in an infant stage." 14. Projects which were reserved for the public sector in

the Second Plan had to be abandoned and were transferred to the private sector. Cohen stated, "The objectives of planning are wider than those which private enterprise has normally in view. The private sector has to become an agency for the furtherance of public ends. But from the Third Plan period, the public sector gained far more importance than was ever given to the private sector.

The planning process results in progress of economic growth and nationalization is one of the methods used to achieve economic growth. To alter the distribution of income in a mixed economy is to nationalize the productive enterprise. Such a measure enables the Government to increase public profit in the national income. It is worthy to note that nationalization in India was undertaken for specific and strictly defined objectives, not as part of an over all anti-private sector strategy. Air transport was weakly organized and so nationalized in 1953. Life Insurance was taken over in January 1956, partly in order to clean up an unusually corrupt and inefficient sector. Kolar Gold Fields were taken over to end an era of exploitation. One of the purposes of the extensive bank nationalisation in India in 1969 was to expand branch banking and to foster the role of banks in promoting development in previously neglected regions and sectors of the economy in particular in small businesses in the rural areas. Between 1969

and 1972, over 3000 new branches were set up throughout India by the 14 newly nationalised banks. The policy of free India has been to take more and more enterprises under direct State control. But at no time was there any hint of confiscation. On the contrary, compensation was generous. A wave of take-overs began to gather momentum.

The Fourth Five Year Plan (1969-74) particularly emphasized this approach. In the words of Smt. Indira Gandhi, then Prime Minister of India, 'We advocate a public sector for three reasons: to gain control of the commanding heights of the economy; to promote critical development in terms of social gain or strategic value rather than primarily on consideration of profit and to provide commercial surpluses with which to finance further economic development.'

The worldwide movement for change in this century is couched in the language of nationalism. This is distinct from the nationalism of the eighteenth and nineteenth centuries. The nationalism of the twentieth century modernizing countries is the nationalism of political consciousness and of the social uplift of all sections of people. The thrust of internationalism is towards solving issues which affect more than one nation; the thrust of nationalism is towards the survival of the nation and the development of its own polity and economy.

The term "nationalization" usually refers to the process of take over of the industries and services by the Government.

17. Dias, Public Corporations in India, p. 54.
from previous owners. This takeover is significant especially as it is generally done on a compulsory basis. Though the owners of an undertaking may well be reluctant to see it taken over by the Government for various reasons, they always receive compensation — mere expropriation is not practiced in India.\textsuperscript{18} The nationalization of private property is a right, now widely recognized by most international lawyers, but its exercise in a legally acceptable way carries with it the obligation of paying compensation to the private interests affected.

Nationalization helps in the process of economic growth and redistribution of income, provided the public sector is run efficiently and is generating some surplus, which could be used for developmental purposes. If the public enterprises are incurring losses, they are likely to retard the economic process and progress. Under these circumstances additional taxes might be necessary to compensate for such losses which might then entail transferring scarce resources from other more productive sources.

The recent spread of public enterprise is one of the most fundamental changes occurring both in the industrial West and the developing countries. One feature of the spread of public enterprise has been the extensive use since the mid-1950s of the policy weapon of nationalization: the acquisition by the State if necessary by compulsion of property formerly owned by private interests.\textsuperscript{19} What is nationalization? The entry of a Government

\textsuperscript{18} Thornhill, \textit{The Nationalized Industries}, p.17.
into a workable joint venture with foreign interests requires the creation of a publicly-owned, semi-autonomous corporation to hold the national share. Such a public corporation, generally free from administrative rigidities has to exercise a great deal of independence in decision making. To ensure its success, it is best operated as a commercial company in terms of management and accounts, with the Government content to play the role of the sole shareholder. Nationalization was to be used as an expedient for increasing production. In Pandit Nehru's words, "Nationalisation was considered necessary to help move the wheels of production and to achieve economic stability. Our policy is to direct our energies in increasing productivity and not in seizing hold of existing institutions and things which are functioning."

However, he emphasised that, "I do not believe in nationalisation as such because when you nationalise, you have got to pay compensation... I do not want anything to be acquired except on payment of just compensation." In most developing countries too, nationalization has generally been concentrated on foreign-owned concerns.

The Socialist theory has been strongly reinforced by economic nationalism through a desire to reduce dependence on private foreign capital and to ensure that the commanding heights of economic activity are under domestic control. Therefore, nationalization has been largely confined to the State acquisition of foreign-owned concerns. It was also agreed that nationalization was to be affected in the case of foreign

interests particularly those involving the utilization of scarce natural resources on payment of reasonable compensation. These State acquisitions have, moreover been amplified by Government initiatives to set up new publicly owned enterprises where none existed before.

Obviously, the effectiveness of nationalization to reduce inequality greatly depends upon whether compensation is paid to the former owner and how much they receive. There are cases where compensation has seemed excessively generous. In the case of foreign investments, the Government is likely to come under strong international pressure to pay full compensation, against the threat of withdrawal of aid and the discouragement of further private investments.

India made little use of nationalization between 1956-72; assets nationalized between 1956-72 were only equal to about 3% of the value of foreign investments there. Yet, it developed a large and growing public enterprises sector from 5 in 1951 to 21 in 1956; from 42 in 1961 to 74 in 1966; to 113 in 1973. Most of these ran public utilities of various kinds. As of March 1973, 66% of total investments in public enterprises in India were concentrated in steel, engineering and chemical industries. The total extent of public funds involved directly or indirectly in manufacturing and commercial activities was around Rs 20,000 crores in the country.

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The birth of the public sector with the definite acceptance of the principle of nationalization together with the general caveat that even those undertakings which operate in the private sector might be subjected to State regulation and guidance made a revolutionary change in the concepts and policies pursued upto that time.

When private undertakings were nationalized or new undertakings were set up in the public sector, the hope was expressed in many countries that the very act of public ownership would usher in a new era of industrial relations. In the United Kingdom, the policy of nationalization started with the desire to improve the lot of workers in the industries taken over. The workers were urged to work in a true spirit of public service. The nation, through the Parliament and the Government, has set up nationalized industries and endowed them handsomely. In return it expects these industries to operate in the national interest. Operation in the national interest means that the industries must provide the national requirement of producing in adequate quantities and at a reasonable price. Nationalization stands justified in the interest of national development, public welfare, public utility or national security.

Arguments about the control of a monopoly have probably been the most frequent element in all the cases where the State

22. Nabagopal das, The Public Sector in India, p. 130.
has taken over or 'nationalized' an industry or an undertaking previously in private ownership. Monopoly in essential services should be curbed. Where monopoly has been created by the Government, it is sometimes done on the grounds of efficiency to prevent wasteful and unnecessary competition. Both economic planning and monopoly justify nationalization because of the power over resources which each gives. Contrary to expectations, the process of industrialization has not increased the autonomy of the developing countries whose technological and capital requirements continue to increase and the dependence, though of a different sort simultaneously increases. Development has generally stimulated the need for more exotic technologies and expertise not readily available in developing countries.

That an industry or service is essential to the effective conduct of war or the provision of an adequate defence system, is another reason for Government control. The Railways were under the immediate control of the Government both in the First and Second World Wars. Atomic energy provides similar arguments. In many developing countries, particularly in the case of crude oil, it was observed that when this industry was run by foreign private investors it was found to be least remunerative for the host Government. Nationalization enabled the Government to assume the heavy capital expenditures necessary to set up manufacturing plants or refineries to make the entire industry profitable to the Government.
So that the public sector does not act too independently, there are a number of legislative and administrative restrictions and its accountability to the Government. Normanton states, "Genuine accountability adds a whole dimension to the idea of nationalization. Without it, nationalization appears almost devoid of practical significance. A nationalized corporation may be more than merely the old crew in new uniforms, but without the saving grace of public accountability, it is often depressingly apt to look and behave like it."\textsuperscript{23}

In the Indian industrial scenario, the public enterprises helped build up the national economy and has now come to occupy an important place. The rationale for the emergence and widening power of the public sector in India is inherent in certain facts like the need for rapid development. National interest requires that the pace should be quickened along harmonious and coordinated development even as some loss occurs in the immediate future. And rapid development must be achieved through the apparatus of the Government. But this does not mean that private sector is to be extinguished. There is scope for the co-existence of both the sectors in a spirit of healthy competition. Public sector requires the co-operation of the private sector to achieve its ambitions, and fulfil its plans, and vice-versa.

\textsuperscript{23} E. L. Normanton, \textit{Accountability and Audit of Governments}, Manchester, 1966, p.368.
The public corporation which takes over an industry from previous owners, acquires both a bundle of assets in the shape of an undertaking as a going concern and a liability either to pay compensation or to assume the outstanding liabilities of the said concern. Various methods are used for calculating the compensation paid to former owners. Payment is made in fixed interest stock in accounts which takes account of the stock exchange prices and the dividends paid over a period prior to the takeover, or the entire industry is valued and a sum is fixed by a Tribunal or through means of mutual negotiations.

This is by no means an easy task and all the nationalized undertakings do not necessarily become successful. The question of the improvement of the public enterprises performance is one of great urgency and efforts should be made to bring this about as quickly as possible. In 1960, Professor J.K. Galbraith who had been invited by the Planning Commission to make a frank appraisal of the performance of Government Undertakings had stated, 'The time had come when the organisational aspect of public sector undertakings should receive much greater attention."24

Closely linked to the subject of nationalization is the issue regarding the right of permanent sovereignty over natural resources. This was a subject of great controversy, having been resolved only when a kind of compromise between opposing

viewpoints of developed and underdeveloped nations emerged. The underdeveloped/developing countries were aiming to secure an international recognition of their right to nationalize and re-establish effectively their sovereignty over the natural resources contained in their territories, regardless of the necessity or adequacy of compensation. The developed nations were willing to recognize this right only on the condition that these nations should make payment of adequate compensation. The driving force behind these efforts of the underdeveloped/developing countries was the fact that during periods of foreign domination, alien economic interests were firmly established in their lands, and economic development agreements were entered into to exploit the natural wealth and resources of these countries. To be able to finance their plans for economic development, they felt it necessary to nationalize these foreign interests and divert the output of their resources wholly to the benefit of their people.

It was argued that the sovereign countries had the right to nationalize and freely exploit their natural resources. The Resolution of December 14, 1962 adopted by the United Nations recognized that nationalization, expropriation and requisitioning were means of exercising the right of permanent sovereignty. Nationalization has been recognized as a measure which is within the competency of a sovereign state to take, if adequate compensation is secured for damaged interests. This was the

beginning of the birth of public sector in the petroleum industry.

This decision was based on three fundamental considerations:

a) Only a publicly - owned company could guarantee that the new resources would be exploited to the full without recourse to restrictive practice;

b) Through a publicly - owned company, the Central Government would receive the mining rents and devote them to purposes in the national interest;

c) The presence of a public enterprise would stop the grouping of private interests which might exert dangerous pressure on the life of a nation.

Let us now delve into the era of oil concessions and market shares when from 1928 onwards to the Second World War and even later, the seven or eight international oil companies, who were then the only ones that counted, held sway over the world oil scene.

These interlocked firms were Exxon, Mobil, Standard Oil of California, Texaco, Gulf, British Petroleum (BP), Royal-Dutch Shell and Compagnie Francaise des Petroles (CFP). The first five are U.S. Companies, British Petroleum is British-owned and CFP is a French Company. Royal Dutch/Shell is 60 percent Dutch and 40 percent British. The concession agreements were signed not as a
result of any weakness in the Middle Eastern politics, but due to the complete novelty of the oil industry, with its particular needs and methods in that area. As per these agreements, the Oil Companies were granted exclusive rights to explore, prospect and drill for petroleum in the area of the concession. They were entitled to carry the petroleum extracted, refine it if necessary, and sell it in domestic and foreign markets. The periods of duration varied in length but were generally characterized by being surprisingly long. The rights of the host Government were very vague and almost non-existent.

The oil concessionary system, that prevailed in the Middle East ever since oil was discovered did not leave much control over the basic natural resource in the hands of the national Governments. The oil companies in a bid to increase their profits vied for more and more concessions and this often resulted in clashes over the issue of the areas of concession.

Around 1947, the oil companies decided to compose their differences on oil concessions and to stay in their respective positions in an 'AS IS' agreement and the understanding on oil concessions, which went with it. Then followed the ten golden years during which was formed the 'image' of international oil as being a closed shop, an oligopoly of sorts, of the Seven Sisters, to use signor Mattei's colourful phrase for these companies.\textsuperscript{26}

As the Second World War drew to a close, two groups sought to organize the world oil market: the major international

\textsuperscript{26} Paul H. Frankel, \textit{Oil - the Facts of Life}, London, 1962, pp.11-12.
oil companies and the United States (U.S.) policy makers. The major international oil companies saw control of the prolific oil fields in the Middle East as the way to ensure their continued dominance over the world oil industry. The U.S. policy makers saw control of petroleum resources as both a source of U.S. power in the post-war period and a way of facilitating recovery in Western Europe and Japan and integrating those areas into a world economy to be centred around the United States of America.

In the post-war economic growth, the substitution of oil for coal and the expansion of ocean and automotive transport were expected to increase worldwide demand for petroleum greatly. In 1950, virtually all the oil produced outside North America and the communist countries was produced by these eight international oil companies. The three best established Exxon, BP and Shell accounted for about 70 percent of this production. These companies till 1975 still accounted for about 90 percent of the total non-North American, non-Communist oil production. These companies were vertically integrated and each operated in the production, transport, refining and marketing sectors of the industry. They sought to maintain a price level that was well above the cost in order to resist encroachment by others into the Middle East Concessions, and to oppose the efforts of oil-exporting countries to alter the concession terms in their favour.

The mid-1950s marked the zenith of the Anglo-American

majors' control over the world oil industry. The demand for national control of the oil fields has a long history. In 1951, the Mossadegh regime nationalized the Iranian oil fields only to give them back three years later to the majors. The Anglo-Iranian Oil Company had negotiated agreements with the Iranian Government which made oil the property of the Company once it had been taken out of the ground and paid for. In other words, Iran had no right to sell its own oil anywhere. The Iranian nationalization dispute established an important precedent for the oil industry. A reformist Government had acted in opposition to the interests of a major oil company and the result was a crippling loss of revenue. The oil activities were completely crippled. The producers were still dependent on the majors' downstream markets, an extremely important potential weapon in the hands of the companies. The weapon was effectively used against Iran in 1953, when after nationalizing the oil industry, the country managed to sell a mere 103,000 tons of crude oil over a period of three years. This was equivalent to one day's output before nationalization. This experience proved to be a powerful deterrent against similar action by other countries. As Geoffrey Chandler, an executive with Royal Dutch/Shell stated, "Throughout the 1960s, the Mossadegh episode in Iran was remembered as indicating an ability on the part of the companies to frustrate the effective exercise of nationalization." 28

Yet the dominance of the international majors did not last long. Their power was challenged by those emerging forces...
that had been excluded from control of the system: the oil exporting countries, which demanded greater revenues and national control and other consuming countries which demanded a greater role in the system. Very soon the private companies and various national oil companies also sought to gain entry into the oil industry, attracted by the huge profits this business offered. By late 1960s the majors' control had been considerably reduced.

In 1961, Iraq nationalized the unexploited acreage in the I P C (Iraq Petroleum Company) Concession. Yet it was Algeria that became the first country to gain national control of its oil industry, followed by Venezuela, Libya, Iraq and others. The combination of emphasis on national development and exploitation of the advantages that non-major companies were willing to provide enabled Algeria to achieve this success. Today the oil industry is nationalised in all the most important exporting countries, and also in most of the oil producing countries.

It was to end the monopoly of the majors that the oil consuming and oil exporting countries thought of concluding agreements with one another. This was the beginning of joint ventures. Till as late as 1969, the leaders of oil exporting countries supported participation agreements as against nationalization proposals. This was particularly desirable if the price structure was to be preserved. But the 1970s saw nationalization proposals gaining support vis-à-vis participation agreements. This was also the period of soaring prices in the world of oil which led to the inevitable oil crisis of 1973.
Iraq, Iran, Kuwait, Saudi Arabia and Venezuela were the founders of the Organization of the Petroleum Exporting Countries (OPEC) when they met in September 1960. Qatar joined in 1961, Indonesia and Libya in 1962, Abu Dhabi in 1967, Algeria in 1969, Nigeria in 1971 and Ecuador in 1973. The thirteenth member is Gabon. The main task of OPEC was to stabilise oil prices. It asserted that 'member countries can no longer remain indifferent to the attitude heretofore adopted by the oil companies in effecting price modifications' 29

In 1971, OPEC demanded that the exporting countries be granted effective participation in the companies oil producing concessions. The majors received a setback by the challenge from the State - backed or State-owned oil companies all over. The majors further suffered because they were divided among themselves, particularly on the compensation issue.

On March 1, 1972, Sheikh Zaki Yamani, the Oil Minister of Saudi Arabia commented: "There is a world wide trend towards nationalization and Saudis cannot stand against it alone". 30 Between 1970 and 1973, Saudi Arabia's share of world oil exports had increased from about 13 percent to about 21 percent. Its reserves were much greater than those of any other country and so the whole world was listening to what the Saudis had to say. But the greatest stumbling block was the technical assistance which

29. S. Manoharan, The Oil Crisis, New Delhi, 1977, p.56.

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was still the monopoly of the international oil companies. Nearly all the countries still required technical aid in oil exploration and production apart from the capital required for these activities.

Sheikh Yamani in January 1973 explained:

"Nationalization does not guarantee the State concerned the means to market its crude. The real problem is how can any State, Arab or otherwise continue to search for new oil resources once it embarks on nationalization. If I nationalize the oil resources of my country, the oil companies will withhold investments for oil exploration and there will be difficulties."

Yet, definite progress was being made. The participation agreements and accompanying nationalizations were significant in several respects. First, they kept the momentum building towards acquisition of greater and greater control and power in the hands of the host country, irrespective of the fact whether it was an oil exporting or an oil consuming country. The demands for participation put an end to any illusion the companies might have harboured on stability. In participating negotiations, the exploited countries showed that they could threaten unilateral action and production cutbacks and that they could exploit the disunity among the international oil companies. By gaining an equity interest in the companies' operations, the countries increased their control over various industry operations. And most significant, by resisting the companies' demand that

compensation be paid for the value of the oil reserves that the companies returned to the exporting countries, they established the claim that national sovereignty meant control over the resources in one's country, irrespective of the fact that the contracts signed in an earlier period had ceded such control to the companies. Yet, the countries acknowledged their continued dependence upon the international oil companies for technological assistance and aid in the marketing of their oil. No wonder, in both refining and retailing the movement towards State control was very slow.

The developments leading to the oil crises of 1973 and 1979 respectively testify to the strength of nationalism. The growth of nationalism in the Third World has been nearly continuous. The efforts of national liberation movements to gain control of their countries has had a continual impact on the international oil industry. Third World nationalism led countries to insist on control over their natural resources, The sign in front of the hotel in Doha, Qatar, where OPEC met in December 1976 proclaimed - "The control of nations over their natural resources is an inalienable right".  

Through sustained efforts exerted in the United Nations in the 1960s, economic nationalism expressed itself in the form of the Right of Permanent Sovereignty over Natural Resources. In the developing countries also, it had been discovered that the colonial period had left them with no effective control over

these resources. Under the internationally recognized doctrine of sovereignty, a State enjoys full and exclusive control within the area of its jurisdiction. Sovereignty itself is of a permanent nature. The Rights of Permanent Sovereignty include right of exploration, development and disposition of natural resources including oil. It was true of events taking place in India as well, where nationalization of the entire oil industry was being speeded up in an effort to gain full control of its natural resources.

The 1979 oil crisis led to a renewal of public hostility and suspicion towards the major oil companies. And as the power of OPEC increased, that of the international oil companies declined. Therefore, while in the sixties, the major international oil companies gained concessions for oil exploration and refining in the underdeveloped/developing countries, by the late seventies, the oil industry had been virtually nationalized. Apart from what has been indicated so far, it has also to be seen that oil production gives rise to large permanent financial surpluses in excess of "average profits". This surplus profit was no more desired to be shared with the foreigners by the countries possessing this national wealth - oil.

National oil companies existed both in the producer and consumer countries. In the sixties and seventies, national oil companies brought about a near instant revolution in the oil
industry, assuming control of volume produced, price charged and customers supported. This transformed the long established concession system, under which major international oil companies signed agreements with host Governments to explore for and produce crude oil.

The developing countries were no longer willing to permit foreign companies to negotiate long-term concession agreements and thereafter, allow them to operate more or less without control or interference from the host Government. The major resources of the subsoil came to be regarded as a part of the public domain not only de jure but in practice, and Governments exercised increasing control over these resources for the realization of national objectives. The long-term contracts or agreements of the foreign investors whose concessions or titles date from an earlier era were renegotiated; special tax laws applying to foreign resources investments were enacted with a view to maximizing the Government's share of the rent from natural resources; and export regulations were imposed with respect to pricing policies and foreign exchange receipts of foreign investors. Gradually, the aim was to achieve complete nationalization of the resources industries. This was the outcome of the widespread feeling of developing countries that foreign investors cannot be trusted to develop their resources in the national interest and so led to demands either for Government ownership or limitation of foreign participation to a minority
role. Nationalization was a part of a struggle waged by the people of the Third World against economic imperialism. Increased pace of State involvement and nationalizations can also be understood as consequent to the spurt in oil prices.

Let us now turn more specifically to the scene in India where the public sector has come to occupy a prominent place in the national economy. India is following the policy of nationalization not by choice but by necessity. It was indicated by the authors of the Second Five Year Plan that, "The public sector has to expand rapidly. It has to play the dominant role in shaping the entire pattern of investments in the economy. In a growing economy which gets increasingly diversified, there is scope for the public and private sectors to expand simultaneously, but it is inevitable that, if development is to proceed at the pace envisaged and to contribute effectively to the attainment of the larger social ends in view, the public sector must grow not only absolutely but also relatively to the private sector. Therefore, the share of aggregate public sector investment in total investment rose from 46 percent in the First Plan to 56 percent in the Second Plan."

Since 1955 there has been a large expansion of the public sector in a wide range of activities, covering mining and manufacturing, generation and

distribution of power, construction, transport and communications, irrigation, banking and insurance, trade and social services. The growth of the public sector has been indeed impressive.

Apart from new undertakings which were being set up in the public sector, the Government embarked upon an era of nationalization, by taking under its control, a number of foreign owned companies or those which were being run inefficiently. The first real major step was taken by the then Prime Minister of India, Indira Gandhi, when on July 19, 1969 fourteen major banks with deposits of Rs. 50 crores and above were nationalized. This was done with a view to achieve progress in the direction of socio-economic democracy. This is through ensuring availability of credit for various types of small producers and other business units. The main arguments offered in favour of nationalization of banks centred around rectifying structural-functional defects of the banking system then in existence. Nationalization was a means to an end, the end to usher in a socialist economy. This apart, it also meant control over policy matters by the Government which was striving hard to gain control over units so far in foreign private hands.

With the ever increasing importance of oil, it was towards this field that the Government now turned its serious attention to. The exploitation of oil resources presents a prime example of the efforts of the developing countries to achieve
economic sovereignty. One of the most valuable and essential natural sources of power in the world, oil requires extremely advanced technical methods of exploration, drilling and production, and heavy capital investment. But the speed with which the State intervened in the oil industry remains, by any standards, exceptional. The 100 percent State - control is the result of a drive for economic independence in the developing countries, particularly since the jump in oil prices following the 1973 OPEC price revolution, and the consequential huge effect that oil, or the lack of it, had on these Countries.

In India, there has been a long struggle over the extent to which the Government could carry out oil exploration on its own, as opposed to granting concessions to foreign oil companies. India was being strongly pressurised by the major oil companies including Exxon and Mobil, the United States, the World Bank, and the International Monetary Fund Agency to leave oil exploration to the private companies. The aim of the oil companies was for complete control or at the most to enter into a joint venture once commercially explorable fields are discovered. In this system, the joint venture takes over production and subsequent phases of development. The profit sharing is generally fixed at 50 percent each.

But the aim of the Indian Government always was for 100 percent control of operations in the field of oil. The trend towards the creation of national oil entities received an overwhelming momentum in the last thirty years or so. One of the
main motives of their establishment was the perception that oil will remain the predominant source of energy in the coming years, and that adequate supply of oil will continue to be essential for economic growth. In this connection, State petroleum enterprises became an important instrument of Government energy policy, in a bid to enforce the principle of Permanent Sovereignty over Natural Resources. These national oil companies brought about a drastic change in the balance of power among those who earlier controlled the world petroleum resources. This gave rise to the development and spread of the public sector in the petroleum industry. Even though India has been producing petroleum since 1890, it was only in 1956 that a wholly owned Indian organisation, the Oil and Natural Gas Commission was established to undertake exploration, drilling and production of hydrocarbons.

State partnership became a condition for obtaining new prospecting licence. Stanvac agreed to associate with the Government in exploitation once commercial quantities were struck in West Bengal; Assam Oil agreed to become a rupee company with one-third Government share in exchange for a twenty year prospecting licence covering 800 square mile area near their new Nakorkatiya field. Initially, the Government assumed a threatening posture. Fortified by the Russian estimate of India's oil reserves, Maulana Azad, then Minister of Scientific Research and Natural Resources demanded 'not one farthing less than 51
percent Indian ownership. Later the Government drew back a bit; simplified licensing rules together with a formal general invitation to foreign private companies' to join the quest for oil in India, subject to mutually acceptable terms. It continued to insist on 'State partnership' half or more than half the profits, and the Government itself having undivided control of any oil found,' showed which way the wind was blowing for the foreign investors. With the exception of a new licence for Oil India in exchange for a rise in the Government's share from one-third to one-half, private companies were virtually excluded from prospecting for, and producing Indian crude.

Refinery profits of the three foreign-owned refineries were scrutinized to ensure that no avoidable drain occurred. Soon, Burmah-Shell and Stanvac surrendered their right to duty protection on motor spirit of 2 annas (12.5 naye paise) per gallon, at a total cost to them of about Rs. 10 crores. K.D. Malaviya, then Minister for Mines and Fuel pressed the companies to replace the existing price formula based on assumed cost by one based on 'actual cost ...... plus reasonable profit'. The companies were asked to justify their product prices which were higher than in neighbouring countries that did not have the benefit of refineries. The companies were informed later in 1958, 'that the Government considered it necessary to examine the

34. Kidron, Foreign Investments in India, p.169.
quantum and propriety of all charges ..... included by them in their selling price of each product'.

No real dent could be made in the pricing formula adopted by the companies until alternative supplies were found. This meant augmenting indigenous crude with imports; building State refineries with Eastern Bloc aid initially, and breaching the companies' monopoly of marketing all of which the Government proceeded to do.

The setting up of refineries was soon taken up simultaneously with the problem of entering the marketing and distribution fields. Direct assault on the companies' monopoly was clearly ruled out; they shared 95 percent of the market, whereas till then the Government had no regular supplies, lacked storage, transport, and marketing facilities. The Government planned to have the distribution of petroleum products in the public sector, this was to be 'in due course and in agreement with the oil companies'. For the moment, the new Indian Oil Company (now Indian Oil corporation) floated in June 1959, would limit itself to supplying Government requirements, or about one-tenth of the total. The only immediate threat to the companies lay in the Government's stated intention to operate through Indian Oil Company before the public sector refineries came on stream.

K.D. Malaviya clarified, "It will be our effort to

control and have a fair share in the work of oil distribution and at the same time to examine it and consult the foreign companies to see that a reasonable scheme is produced so that this work of distribution might be taken up by the Government in a satisfactory manner'.

The source of supplies now became crucial, and the companies pressed for permission to increase production. In June 1959, Burmah Shell offered to forgo another tranche of 'duty protection' in exchange for an additional 300,000 tons a year throughput. This was accepted. A similar bargain was struck with Stanvac, as from October 1, 1959. An Agreement with Caltex in the same vein followed in November 1960.

Meanwhile, the rich Ankleshwar field in Gujarat was struck. Russia made an offer of crude at 15-25 percent below the ruling prices. In light of this offer, the Government raised official objection to the pricing, training and by products clauses of the Refinery Agreements. The Companies were approached to refine Russian crude but they refused. Consequently, Malaviya rejected a Burmah Shell offer to exchange the Refinery Agreement for permission to raise the throughput from 2 3/4 million to 4 million tons a year. The battle continued well into the spring of 1961. Malaviya opened a chink for bargaining by stating that the Government would consider offers for new refineries on condition

40. Kidron, Foreign Investments in India, p.171.
that the foreign share would be a minority one. However, the first proposal to nationalize the refineries made in the Rajya Sabha in December 1961, was turned down because the State refineries were not yet ready to take up large scale operations.

The policy of establishing new refineries wholly in the public sector was reconsidered. An Agreement to build and operate a new 2.5 to 3.5 million ton per year plant at Cochin was concluded with Phillips Petroleum of the United States in April 1963. The Government was to hold 51 percent of the shares, 25 percent was to go to Phillips, 2 percent to Duncan Brothers and the rest to the Indian public. This Agreement set the pattern of negotiations between the Government and other foreign companies towards the end of 1963 for two more refineries to be set up at Madras and Haldia (near Calcutta) respectively.

The foreign oil companies continued to operate but they were made to share, if only in a limited way, the local market for crude and products, to distribute some of their profits within India and were made to come very near indeed to relinquishing the extraterritoriality written into the Refinery Agreements. Their efforts to diversify into the field of petrochemicals in India was a sign of their waning confidence in traditional activities and of profounder trends within the oil industry where the Government was slowly but surely gaining control.

41. Kidron, Foreign Investments in India, p.172.
42. Ibid., p.175.
The Indian Government in its core economic field continued to use foreign capital. Yet it did not embrace foreign capital blindly. Foreign capital could count on being isolated whenever it attempted to retain or create a monopoly position for itself to the total exclusion of Indian interests. Oil is one example. 'Burmah Shell Refineries might find the Government more responsive if they could couple their plans for expansion with an offer to provide for Indian participation in the equity capital of the company. They jolly well deserve the squeeze' commented A.D. Shroff, an arch-critic of the Government but his views were reflective of the views held throughout the Indian business community.43

Subsequently, the Government acquired refining and marketing facilities from transnational and local private owners and constructed additional capacity themselves through Indian Oil Corporation. Until January 1962, when the first State-owned refinery came on stream at Gauhati in Assam, the industry was shared by Assam Oil's fifty year old refinery at Digboi in Assam; Burmah Shell's and Esso - Standard's in Bombay and Caltex refinery at Visakhapatnam. The refining capacity in the public sector was to be further increased by 1966. The companies till such time held control of over half the indigenous output, but their complete monopoly was being breached by the growing public sector. The developments in the Indianization of the oil industry till 1966 are given in the Table below. 44

44. Kidron, Foreign Investments in India, p.194.
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<td>Imports of products</td>
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<td>Foreign Private</td>
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<td>Refining capacity (end of year)</td>
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<td>6.7</td>
<td>17.5</td>
<td>17.5c</td>
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<td>9.6</td>
<td>9.7c</td>
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<tr>
<td>Distribution (excl. bunkers)</td>
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**Note:**
Figures for 1951 to 1961 inclusive and the estimate for 1966 were made available (December 1963) through the courtesy of Shell International Petroleum Company Ltd.


c. Oil Ministry target reported in *Economic Weekly* December 15, 1962,
The Table shows an industry still largely controlled by foreign capital, but in which the State was applying increasing pressure. The State petroleum enterprises were created to provide petroleum products at low prices for internal consumption. These national companies in the petroleum sector were to develop and strive to advise the Government in the development of the national petroleum industry; to explore, produce, refine and market petroleum and its products internally; to supervise or control the activities of non-national oil organizations operating within the national boundaries, (till such organizations are fully nationalized); to explore, produce, refine and market petroleum and its products independently or jointly with an international oil company or with another country's State enterprise; and to assist other countries in the development of their petroleum resources, as mutually agreed upon by the respective Governments.

Indian petroleum industry as it stands today has been able to undertake all these functions through the medium of its public sector corporations, both within and outside its national boundaries. The main objective is to promote speedy exploration and development of petroleum deposits under effective national control and to maximize financial benefits from the exploration activities. This apart, the national oil companies or the public sector corporations have been instrumental in taking over or nationalizing the foreign holdings by virtue of negotiated deals. The poignant sentence of K.D. Malaviya indicates the situation
when the foreign oil companies held sway, when he said, "The State oil industry was forced to start from scratch because the foreign companies had failed to train one Indian technologist throughout the sixty - odd years of their operations in the country."

No wonder, Malaviya was such a staunch supporter of nationalisation of the oil industry. He tended to agree with Abudullah M. Tariki, former Saudi Arabian Minister of Oil, who at the Fifth Arab Petroleum Congress in 1965 argued that "Nationalisation was a national necessity". In 1973, Abdel Rahman Salim al-Atiqi, Kuwait's Minister of Finance and Oil said, "Nationalisation is the right of all countries". ....... a right, which was soon to be exercised by India in its endeavours to take over the entire operations in the field of oil.

45. K.D. Malaviya, Minister of Mines and Oil, Lok Sabha, quoted in Hindu, April 16, 1961.