DIVESTMENT AND PUBLIC SECTOR ENTERPRISE REFORMS INDIAN EXPERIENCE SINCE 1991

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Working Paper No. 272

February 1997

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* Thanks are due to R. Nagaraj, M. Gopala Krishna and participants of an Indo-Australian Workshop at New Delhi for comments on an earlier draft. Needless to add the sole responsibility for any errors rests with me.

ABSTRACT

All over the world there is a pronounced trend towards privatising public enterprises on the ground that it is the best and perhaps the only credible policy for improving the performance of state-owned undertakings. In most developing countries privatisation or reform of the PSEs has become an inevitable consequence of the **structural adjustment programme.** India too has followed a policy of privatisation or more specifically a policy of divesting off government's share holding in a number of enterprises under its ownership. But this policy has been poorly articulated and its implementation very lackadaisical in nature. Consequently very soon the government is going to be left with a number of poorly performing enterprises which will be a drag on its budget while the better performing and dividend paying enterprises would have left its fold. I argue that at the root of this apparent contradiction is the real reason behind the reform process in India. Divestiture is thought of primarily as a mechanism to generate non inflationary form of resources to fill in the burgeoning fiscal deficit of the central government. Improving performance has been the least of considerations. The paper is structured into **three** broad sections. In the **first section** I survey the various public enterprise reform policies initiated and implemented since 1991. They are: (a) policies which has focused on creating domestic competition by eliminating barriers to entry, subsidies, price distortions, and preferential access to budget and bank resources; (b) policies for improving the management of PSEs by increasing or improving their interface with their respective administrative ministries; (c) policies for introducing restructuring and for establishing a social safety net programme; and (d) implementing several rounds of divestment. In the **second section** I argue that the only policy that has been implemented in a significant manner is the last one. Further in the section a detailed critique of this policy is provided. In the **last section** I present a critique of the concept of social safety net in the context of PSE reform process.

JEL Classification: L 32, 33.

Key Words: Privatisation, Divestiture, Public Sector Enterprise Reforms, Memorandum of Understanding, Underpricing, Social Safety Net, National Renewal Fund, Voluntary Retirement Scheme.

The one major policy shift that has occurred in both the developed and developing world is the overriding belief in privatisation as a panacea for the ills confronting public sector enterprises. The genesis of this belief is the commonplace observation that public enterprises are inefficient because they address the objectives of politicians rather than maximise efficiency(Boycko, and Vishny, 1996). If one surveys the trend towards privatisation across a large number of developing countries, the following issues emerge:

(i) Privatisation in developing countries has often been a necessity following pressures from international agencies. According to Campos and Esfahani(1996)for most developing countries, economic downturn may be an almost necessary condition for PSE reform. The reform of the public sector in general or privatisation in particular is an integral component of the structural adjustment programme which most of these countries were made to pursue. This however, has not included guidelines on how privatisation should be carried out and the variations between countries are substantial;

(ii) As a corollary of the above, the main rationale for privatisation is to raise non-inflationary form of revenue to fill in the deficits in especially the revenue budget of the central governments. According to an estimate by the World Bank approximately $96 billion has been raised by developing countries alone during the period 1988-1993[1] ; and

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1 See World Bank(1995), p. 28. Much of these have been contributed by privatisations in Latin America(56%).

(iii) In so far as available evidence makes possible any firm conclusions, the impact of privatisation on the performance of enterprises has been very varied. Even the principal objective of revenue raising may not always have been achieved. However a recent study by Megginson et al (1994)[2] documents significant improvements achieved surprisingly without sacrificing employment security. Their analysis sowed that, post privatisation, the firms increased their capital investment spending, improved their operating efficiency and increased their work force. Further more, the companies significantly lower their debt levels and increase dividend pay out. But most of the firms in their sample were from the developed market economies.

In the context, the purpose of the present paper is to undertake an analysis of the public sector reform process in India set into motion since 1991. In keeping with the objective, the paper is structured into three broad sections. In section one, I survey the various public sector reform measures and in the second one I attempt at a critique of one of the important measures, namely the process of divestment of government's equity in a number of specified enterprises. Finally in the last section I undertake a critique of the concept of social safety net in the context PSE reforms. At the outset it should be made clear that the scope of our discussion is restricted to the public sector enterprises under the ownership of the central government[3].

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2 The study compared the pre and post privatisation financial and operating performance of 61 companies from 18 countries and 32 industries during the period 1961 through 1990.

3 According to the Department of Public Enterprises(1993-94), there are 246 non departmental public sector enterprises under the ownership of the Central government. See for instance Page 6. My analysis is therefore restricted to these enterprises and therefore does not include reforms in the power and telecommunications sector.

I

THE PUBLIC SECTOR REFORM PROCESS IN INDIA

The reform process is of recent origin though following the world-wide trend there have been some feeble attempts at improving especially the interface between government and enterprises through essentially the medium of the Memorandum of Understanding(MoUs). The first explicit articulation of the desire to divest government's equity holding is to be found in the budget(*interim*) speech of 1991-92 where in it was stated that the central government would divest of its equity holdings in a number of its enterprises in favour of mutual funds and financial or investment institutions in the public sector. This divestment, it was argued, would broad-base the equity, improve management and enhance the availability of resources for these enterprises, was also expected to yield Rs 25000 million to the exchequer in that year, namely in 1991-92. This position was subsequently restated in the new industrial policy statement of July 1991 and the budget speech (of the new government) of 1991-92. In addition to the above mentioned details it was further specified in these documents the precise extent of divestment(which was 20 per cent) and that the shares would be sold not only to the public financial institutions but also to the workers in these enterprises and the general public. So the stated objectives of divestment does not refer to the process as a means of improving financial performance of the enterprises. The primary objectives were: (1) to raise resources for the budget which are essentially non inflationary in nature; (2) broad base the ownership of the enterprises which would eventually allow the enterprises to raise resources from the capital market and thereby lower their dependence on budgetary support.

However to increase efficiency, productivity, and competitiveness of the sector a number of other measures were introduced and if one were to summarise them[4], these were policies which have focused on (a) creating internal competition by eliminating entry barriers, subsidies, price distortions, and preferential access to budget and bank resources; (b) improving the management of public enterprises by increasing autonomy and the mandate to become profit-oriented centres; and (c) introducing restructuring policies and establishing a social safety net programme. The progress todate in these three areas of reform are mapped out in Table 1.

Table 1: Progress of Public Sector Enterprise Reform Programme, 1991-1996

Status in 1991	Progress through 1996
Competition policies	
The number of industries reserved exclusively for the public sector reduced to 18;	The number of industries reserved for the public sector reduced to 6. Private participation in some of these sectors is also permitted on a case by case basis; The question of withdrawing the public sector from non-core and non-strategic areas will be examined;
The direct budgetary support to public enterprises worked out to 1.5 per cent of GDP and they received in addition a variety of subsidies and subsidised credit.	The budgetary support curtailed to 0.8 percent of GDP, financing in domestic capital markets increased, preferential access to bank credits eliminated;
	The PSEs which are operating in commercial areas are expected to pay a minimum dividend of 20 per cent;

4 This summary is based on Chopra, Ajai et al(1995), pp. 62-66.

Management policies	
Direct supervision of public enterprises from government; The MoU system was introduced in 1988-89 and revised in 1989-90 to improve the performance of PSEs by bringing about a proper balance between accountability and autonomy.	Managerial autonomy marginally improved through the MoUs. 99 signed in 1994-95. The financial performance of these enterprises have been better than what had been targeted for in the MoUs by about 8 per cent;
Restructuring policies	
The provisions of the Sick Industrial Companies(Special Provisions), 1985 was amended in December, 1991 to extend it to government companies. 47 central PSEs have been registered with the BIFR(as on 31-3-1991);	Up to the end of March 1995, 53 cases of central PSEs have been registered with BIFR.
There was no social safety net of any sort for unemployment.	A **National Renewal Fund** has been established. But the total amount under this fund is not known[See Section iii for the details]; Participation of workers in the management of profit making and efficient companies will be encouraged.

Sources: 1. Adapted from Table 7.8 in Chopra, Ajai et al(1995), p. 65;
2. Government of India (1995-96), p. 113 and p. 120;
3. Department of Public Enterprises (1993-94), p. 160-163;
4. United Front(1996).

I now discuss the progress of these various reform measures in some detail.

An area where much progress has been achieved is in the area of competition policies where the number of industries that were exclusively reserved for public sector investment has been progressively reduced to 6 from 18. As of now the only industries where public sector can have a monopoly are defence production, atomic energy, coal and lignite, mineral oils, railway transport, and radio active materials. As a result of this policy of deregulation public sector now face competition in areas like power, telecommunication, air transport, oil refining, and mining in general. This coupled with reduction in the budgetary support has further put pressure on the enterprises to be more efficient. A second area of reform has been in effecting more managerial autonomy through the medium of MoUs. According to the Department of Public Enterprise(1993-94), "MoU is an instrument which defines clearly the relationship of PSE with the government and clarifies the respective roles of the PSEs as well as the government in order to achieve better performance. It is also an attempt to bring a proper balance between the accountability and autonomy. The emphasis is on achieving the negotiated and agreed objectives rather than interfering in the day-to-day affairs"[5]. The system has been in existence since 1988-89 and it has progressively covered nearly 40 per cent of the PSEs[6]. One of the difficulties with this exercise has been the lack of credible sanctions against the management that fail to meet commitments in an MoU[7]. Another drawback is the conflict of interest inherent in an administrative ministry rating and supervising the public enterprises that fall under its jurisdiction. In

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5 See Page 160.

6 With this the entire public sector except the enterprises which are chronically sick or of insignificant size would have signed MoUs with their respective administrative ministries/departments. See Department of Public Enterprises(1993-94), p. 161.

7 See Chopra, Ajai et al(1995), p. 64.

1993-94, for instance, 75 per cent of the evaluated PSEs were rated *excellent* or *very good* and only 10 per cent were rated *fair* suggesting that the criteria for ratings were not very stringent[8]. Thus it has run the risk of merely degenerating into a mere administrative ritual. I shall further illustrate this point in the second section that the operational performance of the concerned enterprises have not improved significantly since the introduction of this system. But the approach in principle is sound and can possibly strengthened with more comprehensive mutilayer contracts that further improve incentives, flexibility and, accountability. Finally the last area of reform has been in the area of restructuring the so called sick PSEs. The first step in this direction was to bring the sick PSEs under the provisions of the Sick Industrial Companies Act(SICA). The government policy on sick enterprises was announced in the new industrial policy statement of 1991 in that, " PSEs which are chronically sick and which are unlikely to be turned around will, for the formulation of revival/ rehabilitation schemes, be referred to the BIFR or other similar high level institutions created to protect the interest of workers to be affected by such rehabilitation packages". As per the amended SICA, 53 PSEs belonging to the central government were registered with the BIFR[9]. Their current status(as on 31-03-1995, the latest period for which such data are available) is outlined in Table 2.

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8 A fine critique of the MoU approach is available in Sankar, T L (1990), pp. 71-78.

9 It must be poited out that the RBI has constituted a small working group to explore the possibilities for establishing an independent organisation for undertaking the sale assets of sick PSEs recommended for winding up by the BIFR. But so far no concrete steps have been initiated in this direction. See Rajaya Sabha Unstarred Question No: 966 reported in Assocham (1996), p. 379.

Table 2: Current Status of Sick PSEs (as on 31-03-1995)

Status	Number of PSEs
Recommended for widing up	5
Winding up Notices served on	5
Revival package approved	8
Stay of proceedings by High Court	2
Cases under enquiry	23
Total	**53**

Source: Mohan (1996). p. 78

The Table shows that not a single enterprise has actually been closed down because of protracted legal proceedings. One major bottleneck which hampers progress in this direction is the absence of a credible social safety net. Since this issue has become very contentious I take it up for detailed discussion in the third section. It should however be mentioned that the blame for having such a large number of sick firms does not entirely lie with the public sector for a run through the list of this 47 shows that a majority of them are nationalised private sector companies which were already sick at the time of their take over. Needless to add reforms in this area should also include development of methodologies for identifying loss-making enterprises at an early stage rather than when they are already chronically sick.

From my brief survey of the PSE reform measures, the following issues emerge:

(1) Considerable headway has been made in competition policies. No doubt their ultimate success will depend on the speed with which private sector enterprises can enter the new areas that are now open to

them and offer a credible threat to PSEs; (2) The system of MoUs requires a thorough overhauling. It could perhaps be strengthened with more comprehensive multilayer contracts that further improve incentives, flexibility, and accountability; (3) Some progress has been achieved in identifying chronically sick firms but no fundamental restructuring has actually taken place essentially because of the absence of a credible social safety net which can actually rehabilitate the affected labour in a significant manner.

But as argued earlier the most significant reform measure is the one relating to the divestment of share holding in specified enterprises. I had also argued that the divestment programme may not actually lead to an improvement in the efficiency of the divested enterprises because in any case they were the best performing enterprises in the public sector portfolio: the objective of raising revenue has superseded the objective of improving efficiency. In the following section I subject this to a detailed empirical scrutiny.

II

AN ANALYSIS OF INDIA'S DIVESTITURE PROCESS

The one reform measure that has been somewhat consistently pursued is the divestiture process. Since the main objective of this exercise has been to raise revenue this process has not led to any performance improvements. I organise the discussion of this issue into two subsections. First I present a picture of the nature of divestiture itself since 1991-92 and until the latest one. This is followed by an analysis of the success of this policy interms of: (a) its ability to raise resources for the budget; and (b) its effect on the financial performance of the divested enterprises.

The nature of the divestiture process

The process commenced in 1991-92. After much discussion, the Department of Economic Affairs recommended the following procedure:

(1) The PSEs to be divested will be selected by the Department of Public Enterprises(DPE); (2) The selected enterprises will be placed in three categories(i) very good, (ii) good; and (iii) average; (3) Bundles(baskets) consisting of different combinations of 6 to 9 PSEs would be made including some from each of the very good, good and average categories; (4) The criterion to be used for classifying a PSE as very good, good or average was the PSEs Net Asset Value(NAV) per share of Rs 10- face value---very good(NAVof Rs 50+), good(NAVof Rs 20-49) and average(NAVof Rs 10-19); (5) The particular combination in each bundle would also be decided by the DPE[10]; (6) The bundles were generated in computer and offered for bidding to short listed financial institutions and mutual funds. These institutions were allowed to unbundle them and sell individually in the stock exchange; and(7) The pricing formula adopted for the referral price was average Net Asset Value and the Profit Earning Capacity Value methods.

Divestiture up to 20 per cent of the share capital held by the government in 30 enterprises was done in two phases in December 1991 and February 1992 ensuring that the government's equity would not fall below 51 per cent. Subsequently there were divestitures in 1992-93, 1993-94, 1994-95 and 1995-96. More or less the same procedure was followed in all these divestitures though the divestiture of 1991-92 attracted a fair amount of criticisms from even governmental agencies such as the

10 The reason for selling shares in bundles rather than singly was because it was feared that if equity of individual PSEs was divested separately, then only the very good may be picked up with significantly lower prices and possible no takers for the good and average PSEs. Since wider participation in PSE equity was an important objective of the policy it was felt that it was important to ensure that a wide range of PSE shares were effectively divested. Hence the conscious decision to sell in bundles. See the full text of the speech made by then Finance Minister in the Rajya Sabha on 6-08-1993 while initiating the debate at the calling attention motion on the subject" Situation arising out of large scale divestment in Public Sector Undertakings". See Assocham (1993b), p. 857.

Comptroller and Auditor General[11]. I will be taking up these in the subsequent sub section. In 1993-94 the government appointed a committee under the chairmanship of Professor Rangarajan known as the ***Committee on Disinvestment of Shares in Public Sector Enterprises.*** The report covered various aspects of divestiture such as criteria for selection of PSEs for divestiture, *modus-operandi* of divestiture, criteria for valuation of shares, target clientele for divestiture and other issues. The main recommendations of the Committee are summarised in Table 3.

Table 3: Main Recommendations of the Committee on Disinvestment of shares in PSEs

Recommendation	Scope
Limit of equity to be divested	In general, the percentage of equity to be disinvested should be under 49% in industries reserved for public sector and over 74% in other cases.
Criteria for Valuation of shares	The discounted cash flow method is preferred. Each enterprise would need to be studied carefully taking into account factors such as value of assets, its market share, potential profit earning capacity and the prevailing price in the market for shares of similar enterprises in the private sector.

11 See CAG Report No: 14 of 1993.

Preparatory steps	These include conversion into company form, deciding the desirable levels of equity and restructuring the financial aspects with a proper debt/equity gearing
Modus operandi of divestment	Once a reasonable market price is established in a normal trading atmosphere over a reasonable period of time, the fixed price method would be appropriate.
Standing Committee on Public Enterprise Divestment	Creation of the Standing Committee to recommend enterprise -specific action for reforms, restructuring and divestment as well as monitoring and evaluating the process of implementation

Source: Assocham (1993a), pp-731-32.

The Report was submitted to the Ministry of Finance in April 1993 but it is feared that the recommendations have not yet been adopted by the government[12]. Finally in the budget speech of 1996-97 the government has approved the proposal to establish a Disinvestment Commission which will be charged with the responsibility of taking any decision with respect to divestiture *in a transparent manner*. But, from current press reports, the commission is yet to take off[13].

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12 See Chopra, Ajai et al(1995), p. 66.

13 From current discussions it is feared that the Commission with one full time Chairman and four part time members is very likely to go the MRTPC way as its advice is only recommendatory in nature. But an area in which the Commission has shown some impact is . initiating a wider debate, among all concerned, on several issues connected with divestment such as restructuring of PSEs before privatisation and on the methodologies to be adopted for the optimal valuation of the PSE shares.

Though there has been several rounds of divestiture during the period 1991-92 through 1995-96, major divestiture took place only in 1991-92. See Table 4 for a summary picture.

Table 4: Summary of PSE Divestment, 1991-92 to 1995-96

	Unit	1991-92	1992-93	1993-94	1994-95	1995-96
No of PSEs	Number	30	16	5	16	2
Number of shares sold	in millions	872	449	114	27	na
Targeted divestiture proceeds	Rs. million	25000	35000	35000	40000	70000
Actual divestiture proceeds	Rs. million	30380 (+22)	19120 (-45)	22910 (-35)	26180 (-35)	3570 (-95)
Average price per share	Rs	61.70	42.58	200.96	814.3	na
Range of equity divested	in per cent	0.12 to 20.00	0.11 to 10.00	.01 to 18.57	.01 to 23.1	na

Note: 1. Figures in brackets indicate the extent of short fall, in per cent, of actual proceeds compared with their respective targets.

Source: Government of India(1995-96), p. 121
Mohan (1996), p. 80

Altogether government's equity ranging from as little as 0.26 to 43.1 has been sold involving 40 enterprises(Annexure 1). The only two enterprises where the government equity has come down to the 51 per cent mark are the two refineries, Madras and Cochin. Both these, in any case, had government equity holding of only 85 and 61 per cent respectively in 1991. The very sharp increases in the average price per share in 1993-94 and 1994-95 were contributed by the very high average per share obtained by two enterprises namely Hindustan Petroleum (Rs 1260.01) in 1993-94 and ONGC (Rs 1535.0) in 1994-95. Five major inferences can be drawn from the divestiture exercise.

The ***first*** is that only in two enterprises (namely in HPCL and HOCL) that the extent of divestiture exceeds 40 per cent of government's equity. At least in half the number of enterprises the divestiture works out to less than 10 per cent. See Figure 1.

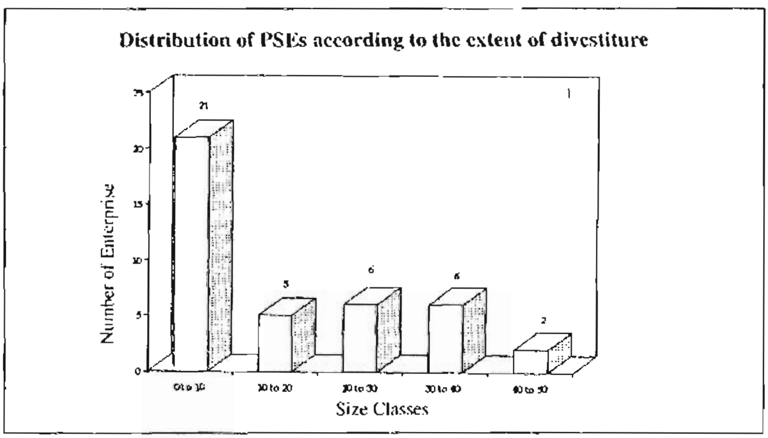

Figure 1

Secondly even though there has been shedding of government's equity the effective control and management of the enterprises still lie with the government. ***Thirdly***, only in three enterprises that the divestiture took place in three of the five years[14]. ***Fourthly,*** the bundling of shares

14 They are BHEL, Hindustan Petroleum and SAIL.

in 1991-92 generally sought to depress the price of all the enterprises across the board. This is brought by the very sharp increases in prices of all the prices in 1992-93 (Figure 2) when the shares were unbundled and sold to the general public as well.

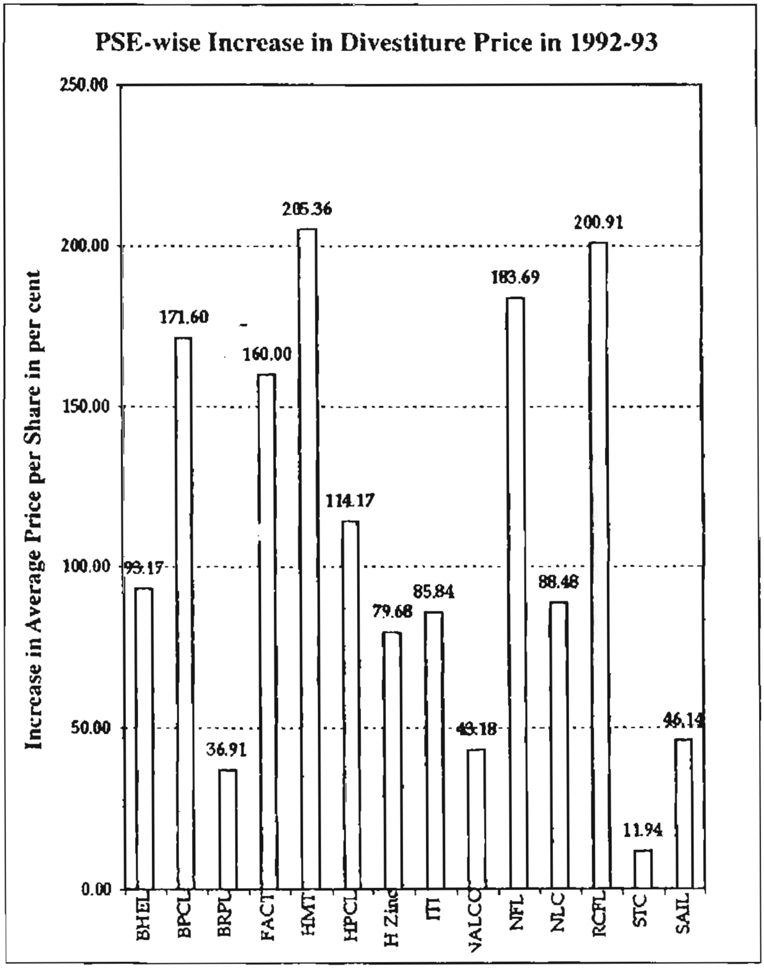

Figure 2

Finally, most of the divested companies, with some minor exceptions, are the most profitable and dividend paying companies to the exchequer. In fact they together contributed on an average 85 per cent of the total dividend paid by all PSEs during the last three years (Table 5).

Table 5: Share of Divested PSEs in Total Dividend paid by All PSEs

(Rs in Million)

Year	All PSEs	Divested Enterprises
1991-92	6872	**5776 (84)**
1992-93	7916	**6787 (86)**
1993-94	10145	**8735 (86)**

Note: Figures in brackets indicate percentage share of all PSEs.

Source: Annexure 2

This raises the issue that for some current revenue the government is going to loose future yield of dividend from these enterprises to the extent that the government equity stands reduced. Questions have also been raised as to the health of the primary market, namely that it was not good enough for divestitutre. This does not appear to be a plausible reason because the public issues launched by private sector enterprises have registered significant increases during the period consequent to the abolition of the Controller of Capital Issues which gave freedom to the sector interms of pricing and the quantity to be raised[15].

Divestiture proceeds

The main purpose of divestiture is to raise revenue for the budget. But even from this narrow objective, the divestiture has fallen short of

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15 For instance, the public issues(both equity and debentures) registered an increase of 191, 31 and 36 per cent in 1992-93, 1993-94 and 1994-95 respectively. See Government of India (1995-96), p. 120

the targeted amount in *four* of the five years and that too by a wide margin. See Figure 3.

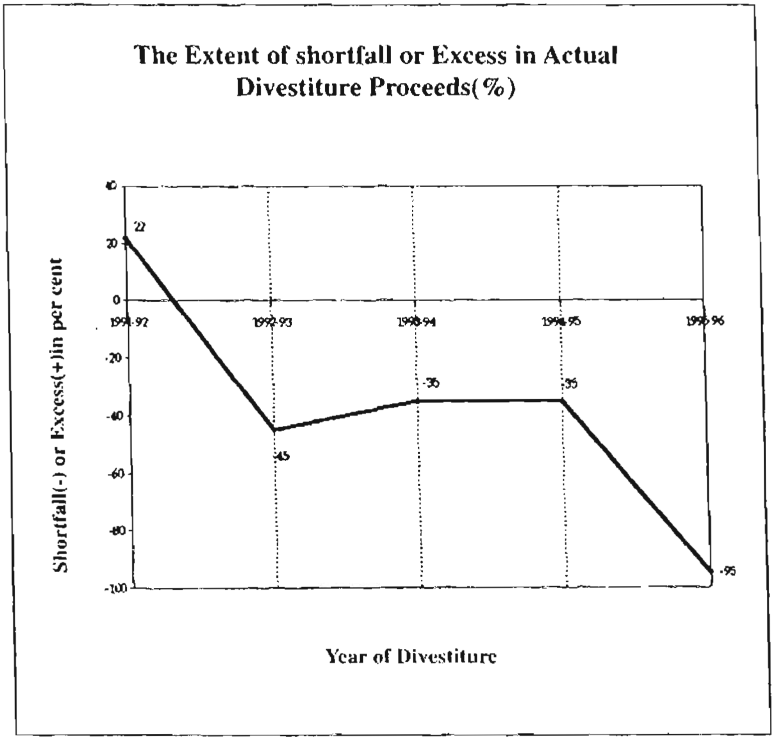

Figure 3

It is seen that only in one of the five years. namely in 1991-92 that the actual proceeds have exceeded the targeted amount. But it is shown by the CAG that that the government could have still obtained much higher proceeds had they priced the shares properly. Consequent to this *improper pricing* the exchequer has lost a large sum of money. There are various estimates of this so called improper pricing. But I restrict myself to basing the discussions on the official computations of it by the CAG. See Table 6.

Table 6: Extent of Loss to the Government in the Divestiture of 1991-92

Name of the PSE	Average price at which share value of Rs 10/ - was sold to financial institutions	Average Market Price per share
1. BPCL	243.89	**962.50 (207.52)**
2. BHEL	38.05	**165.00 (267.94)**
3. HCL	25.17	**62.50 (148.31)**
4. HOCL	56.92	**177.50 (152.55)**
5. HPCL	242.70	**875 (126.62)**
6. HZL	21.65	**56.25 (159.82)**
7. HMT	18.11	**76.25 (321.04)**
8. SAIL	13.24	**60.62 (217.22)**
9. RCPL	9.87	**48.00 (343.26)**
10. NLC	11.46	**82.00 (615.53)**

Note: Figures in brackets indicate the per centage of loss to the government

Source: Comptroller and Auditor General(1993), p. 47

This shows that loss to the exchequer has been considerable[16]. Vaidya(1995) has provided some alternate estimates of the extent of loss suffered in the 1991-92 divestiture. He also estimated that losses were

16 This point is elaborated further in Mani(1994) and Mani(1995).

made in the subsequent sales though its extent had been reduced. It is significant that the undervaluation of shares happened despite the government receiving expert advice on valuation from one of the best, internationally known, private consultancy firms[17].

Further there was also no "claw back" provision which would have granted the government with an opportunity for sharing in any profits which successful bidders may receive consequent to their onward sale of shares. The CAG also pointed out number of other irregularities in the sale[18]. The practise of using a capital receipt like the divestiture proceeds to meet partially revenue expenditure and the levels of revenue expenditure not having been reduced ,the objective of raising non inflationary resources was also not achieved. During the entire period divestiture proceed accounted for a mere 4.36 per cent of the fiscal deficit[19]. See Table 7.

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17 The underpricing of PSE shares is sometimes dismissed of as an inevitable consequence of the complexities involved in its pricing. Even in the UK where the privatisation exercise is generally hailed as a success story, there have been instances of gross undervaluation. Similar experiences have been reported from elsewhere in Europe. The question of how to price candidates for privatisation will be raised time and again. But this question has no easy answer. When a government sets a price for a PSE, it is trying to satisfy people with a variety of interests: institutional and retail investors, taxpayers, the company's employees and, not least, its managers. These interests often conflict. See Economist (1996), pp. 99-100.

18 See CAG(1993), pp. 16-48 for the details.

19 Gouri (1996) also makes this point. See p. M-66.

Table 7: Fiscal Deficit, Revenue Deficit and Divestiture Proceeds, 199192 to 1995-96 (Rs in Million)

	1991-92	1992-93	1993-94	1994-95	1995-96
Fiscal Deficit	363230	401730	602570	610350	576340(BE)
Revenue Deficit	162610	185740	327160	341320	355410(BE)
Actual Divestiture proceeds	30380 (8.36)	19120 (4.76)	22910 (3.80)	26180 (4.29)	3570 (0.62)

Note: Figures in brackets indicate proceeds as a per cent of the fiscal deficit.

Source: Government of India (1995-96). p. 18.

The Table thus confirms the view that even as a *resource-raising exercise*, the divestiture process has been, by and large, a failure. Further, the sale of PSE shares being limited to a number of financial institutions/ mutual funds/merchant banks excluding the workers/employees of the PSEs and the general public could also not be considered as wider public participation as it was claimed in the new industrial policy statement. The policy on the use of the divestiture proceeds has undergone some change from the proposed divestiture of 1996-97. The Finance Minister in his budget speech for 1996-97 has said that the proceeds will be utilised for allocations for education and health in backward areas and for creating a fund to strengthen public sector enterprises. However there is no mention of it in the budget speech of 1997-98.

Financial performance of the divested enterprises.

I have done an exercise, of admittedly limited validity, analysing the performance of divested enterprises pre and post divestiture. For this exercise I have taken only the thirty enterprises which have undergone some divestiture in 1991-92. I computed one measure of profitability, namely the rate of net profit margin(net profit/net sales*100) during three years prior to divestiture(1989-90 to 1990-91) and three years post divestiture(1991-92to 1993-94). See Table 8. No attempt is made to arrive at a weighted average for the entire sample as data on weights(share of each enterprise in the total divestiture proceeds was not immediately available).

Table 8: Financial Performance of Divested Enterprises, Pre and Post Divestiture

Name of Divested Enterprise	Pre Divestiture	Post Divestiture
HPCL	3.24	**1.83**
BPCL	2.72	**2.08**
BEML	7.37	**5.33**
VSNL	21.23	**17.86**
BHEL	4.07	**3.39**
SCI	7.17	**7.75**
IPCL	9.18	**5.47**
BEL	4.43	**4.84**
ITI	3.73	**4.92**
HOCL	12.56	**11.66**
MRL	3.73	**3.32**
MTNL	95.74	**10.10**
HZL	14.23	**14.28**
BRPL	7.65	**9.56**

CMC	0.25	**-0.34**
HPFL	3.79	**-15.25**
AYL	2.72	**2.30**
CRL	4.36	**4.23**
STC	1.55	**1.59**
RCFL	4.91	**1.26**
HMT	0.86	**1.86**
SAIL	3.63	**3.93**
NLC	19.47	**17.11**
HCL	3.31	**-1.78**
NALCO	19.73	**9.74**
NFLC	1.01	**6.40**
FACT	1.30	**2.86**
DRCL	22.9	**16.47**
MMTC	44.97	**1.43**
IRCON	-905.74	**-2207.51**

Note: The firms are arranged in a descending order according to the extent of divestiture.

Source: Computed from data provided in DPE , Various issues.

The Table is very revealing. Excepting for 9 enterprises, the performance has actually deteriorated consequent to divestiture. I of course do not attribute this worsening off to just divestiture. All that one can say is that at least in the short term there is only a worsening despite the existence of a number of *performance enhancing measures* such as the MoUs etc.

III

SOCIAL SAFETY NET AND PRIVATISATION

An important consequence of privatisation and other enterprise reform measures is the rationalisation of the workforce: the workforce is normally reduced. This is based on the assumption that the PSEs are usually overmanned though enterprise-wise estimates of the extent of overmanning are rarely available. The one way of mitigating the sufferings of the workforce that is likely to be shed is to have a credible social safety net by which the affected labour could be compensated at least financially. It is against this background that the central government has introduced the concept of a ***National Renewal Fund(NRF)***. The Fund was established in February, 1992 supposedly to " to protect the interests of workers affected by modernisation, technology upgradation and industrial restructuring". The specific objectives of the NRF are to provide[xii]: (1) assistance to firms to cover the costs of retraining and redeployment of employees arising as a result of modernisation and technological upgradation of existing capacities and from industrial restructuring(x1); (2) funds for compensation to employees affected by restructuring or closure of industrial units, both in the public and private sectors (x2); and (3) funds for employment generation schemes in both the organised and unorganised sectors(x3). An ideal or a credible social safety net should have a corpus of funds sufficiently large enough to finance adequately the three components.

However right through inception the NRF got narrowly equated with meeting expenditure on Voluntary Retirement Scheme(VRS) of central PSEs alone[21]. The main criticism against this Fund is that there is precious little discussion within government circles as to what should be the ideal size of this fund to effectively rehabilitate the affected workforce from not only central PSEs but also Sate level PSEs and the private sector as well[22]. This is clearly borne out by the fact that in 1992-93 against a budgetary provision of Rs 2000 million, Rs 8297 million was actually spent and in the subsequent year against a provision of Rs 7000 million the actual spending Rs 10200 million. This clearly shows the NRF is not adequately funded. In fact there is no fund as such and it is purely based on an year to year allocation. This can be gauged from the budgetary allocation for 1993-94 and 1994-95. See Table 9.

Table 9: Allocation under the NRF (Rs in Million)

Particulars	1993-94(Actual)	1994-95(Budgeted)
VRS in Central PSEs	8300	5000
Worker's Compensation payment in case of closure/rehabilitation and VRS in State PSEs	1400	1500
Worker's Counselling and Retraining programme	500	500

Source: DPE (1993-94),p. 195-196.

It is seen that much of it is for the terminal payments under the VRS scheme alone. Retraining etc. has taken the lowest priority. In fact

21 The VRS has been in existence since 1988-89 in central PSEs. About 99,000 employees have opted for retirement under the scheme from 1989-90 to 1992-93. See DPE (1993-94), p. 153.

22 For an exercise in this direction, see Manit 1994).

it is seen that a good number of the employees of the central PSEs who have opted for the VRS are the younger and qualified ones who inturn have sought employment in the private sector[23]. Second, much of the VRS expenditure has been concentrated in the heavy industry and textile sectors. See Table 10.

Table 10: Industry-wise Distribution of Expenditure under the VRS (Rs in Million)

Industry	1993-94	1994-95	1995-96
1. Heavy Industry	1791	852	64
2. Textiles	1300	400	100
3. Mines	825	350	-
4. Chemicals and Petrochemicals	412	255	-
5. Steel	340	370	110
6. Shipping	362	171	-
7. Defence	100	122	-
8. Aviation and Tourism	86	-	-
9. Civil Supplies and Public Distribution	70	-	-
10. Water Resources	60	-	-
11. Atomic Energy	50	50	-
12. Food Processing	20	-	-
13. Fertiliser	5	30	44

Source: Assocham (1995), p. 637-638.

It can be argued that with the implementation of this scheme under the current procedure, it can be argued that the Indian PSEs are going to loose their best men to the private sector. And as seen earlier in our discussion of the divestiture process the government is going to loose its better performing enterprises too. So at the end of the day, the government is going to be left with mostly the less profitable and loss making enterprises and which are likely to exert a greater drag on its budget. If that happens, it would go a long way towards vitiating the very purpose of the reform process.

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Annexure 1

The Extent of Divestiture(%)

Name of Enterprise	Before Divestiture	Current Position	Extent of Divestiture
HPCL	100	51	49.00
HOCL	100	56.9	43.10
BEML	100	60.08	39.92
IPCL	100	61.43	38.57
MTNL	100	65.73	34.27
BPCL	100	66.2	33.8
M Refineries	84.62	51.8	32.82
BHEL	100	67.72	32.28
IDBI	100	72.14	27.86
B Refineries	100	74.47	25.53
H Zinc	100	75.07	24.93
BEL	100	75.86	24.14
Container Co	100	76.92	23.08
ITI	99.65	77.02	22.63
SCI	100	80.12	19.88
VSNL	100	82.02	17.98
CMC	100	83.31	16.69
NALCO	100	87.15	12.85
Hindustan Photo	100	87.47	12.53
SAIL	100	88.93	11.07
ITDC	100	89.97	10.03
HMT	100	90.32	9.68
STC	100	91.02	8.98
Indian Oil	99.88	91.04	8.84
Andrew Yule	71.3	62.80	8.50

Annexure 1 (contd.......)

RCFL	100	92.60	7.40
NLC	100	93.29	6.71
Cochin Refineries	61.16	55.04	6.12
Engineers India	100	94.01	5.99
GAIL	100	96.63	3.37
NFL	100	97.65	2.35
ONGC	100	96.12	3.88
HCL	100	97.97	2.03
NMDC	100	98.38	1.62
Dredging Corpor	100	98.58	1.42
FACT	98.69	97.35	1.34
Hindustan Copper	100	98.88	1.12
Kudermukh	100	99.03	0.97
MMTC	100	99.33	0.67
IRCON	100	99.74	0.26

Note: Before Divestiture-as on 31/03/1991 and Current Position -as on 31/3/1996

Source: Government of India (1996-97), p. 121.

Annexure 2

Dividends paid by the Privatised Public Sector Enterprises (Rs in Crores)

	1991-92	1992-93	1993-94
HOCL	7.40	7.40	7.40
BEML	4.05	4.50	4.50
HPCL	19.15	25.54	31.92
IPCL	27.9	37.52	40.7
MTNL	36	48	60
BPCL	15	16.5	16.5
M Refineries	23.97	28.53	28.53
BHEL	36.71	36.71	36.71
B Refineries	9.99	9.99	13.98

Annexure 2 (contd.......)

BEL	12.8	12.8	12.8
H Zinc	41.16	26.47	0
Container Co	0.5	1.75	2.6
ITI	10.56	14.08	17.6
SCI	16.94	28.23	42.35
CMC	0	0	0
VSNL	24	24	24
NALCO	0	15.46	25.77
Hindustan Photo	0	0	0
SAIL	79.63	79.72	159.43
ITDC	0	1.44	1.95
HMT	5.21	0	0
STC	9	9	9
Andrew Yule	2.4	1.91	1.9
RCFL	11.03	11.03	
Cochin Refineries	14.48	16.54	17.92
Engineers India	1	2	2
NLC	0	0	0
Indian Oil	40.68	49.31	49.31
GAIL	0	20	30
NFL	21.59	24.53	49.06
ONGC	61.71	61.71	61.71
HCL	0	0	0
NMDC	26.43	26.43	26.43
Dredging Corpor	2.8	3.08	3.36
FACT	0	0	0
Hindustan Copper	0	0	0
Kudermukh	0	19.04	19.03
MMTC	15	15	15
IRCON	0.49	0.49	62
Total for the above	**577.58**	**678.71**	**873.46**
Total for all PSEs	**687.22**	**791.58**	**1014.47**

Source: DPE, Various Issues.

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