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Disinvestment of Public Sector Units in India: A Strategic Analysis

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ABSTRACT

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I. INTRODUCTION

The economic reforms of 1991 on industry was focused on dismantling the edifice of industrial licensing, removing import-licensing from nearly all manufactured intermediaries and capital goods and relaxation of restrictions on inflows of foreign investment. The reform process also started the process of disinvestment of public sector undertakings, thus reversing the balance of ownership in favor of the private sector. Reform process was carried out the assumption that removal of industrial licensing, changing ownership in favor of private sector, opening the economy to the free flow of investment by foreign companies, opening areas hitherto reserved for the public sector to private sector and reducing import and export duties and such other barriers to the free flow of technology capital and foreign trade, etc., all these measures will result in achieving the objectives of development and accelerating the process of integrating the economy with the world economy. It was believed that the cure to all the ills of the economy lies in strengthening the process of liberalization, privatization and globalization

Public Sector Policy in India

The founding fathers of our republic used the public sector as an essential and vibrant element in the building-up of India's economy. Though the public sector units have contributed heavily to develop the industrial base of the country, a number of problems have begun to manifest themselves in many of the public enterprises. Serious problems have been observed in the insufficient growth in productivity, poor project management, over-manning, lack of continuous technological upgradation, inadequate attention to R&D and human resource development. The low rate of return on capital invested has inhibited the ability of public enterprises to regenerate themselves in terms of new investments as well in new technology development. This resulted in many of the public enterprises becoming a burden rather than an asset to the government. In the Sixties and Seventies, the public sector policy has been largely guided by Indian Policy Resolution of 1956 which gave the public sector a strategic role in the economy. However, the policy resolution of 1991 adopted a new approach and reduced the areas reserved for Public Enterprises from 29 to 8. The main dimensions of the new approach were:

- Public enterprises were to focus on strategic, high tech and essential infrastructure.
- Sick Public enterprises to be referred to the Board of Industrial and Financial Reconstruction (BIFR), which would suggest remedies for their rehabilitation or Recommend closure.
- A part of Public enterprise equity to be offered to mutual funds, financial Institutions, general public and employees.
- Public enterprise boards to be made more professional and give greater powers.
- Performance improvement to be secured through the Memoranda of Understanding.
- The government would ensure that PEs were run on business lines as envisaged in the Industrial Policy Resolution of 1956.

II. DISINVESTMENT POLICY

The New Industrial Policy of 1991 is governed more by the philosophy of market forces rather than planning. This policy has initiated five types of reforms: dereservation; disinvestment; performance contract system; review of sick units; and enhanced autonomy to public enterprises. Out of these disinvestment emerges as the most favored reform by the government. The policy of Government on disinvestment has matured over a period of time ranging from 1991-92 to till now. Broadly speaking, the policy can be divided in three phases:

a. First phase from 1991 to 1996: The first policy on disinvestment was announced in 1991-92 by the then Finance Minister Man Mohan Singh. Later in Budget speech of 1991-92 eligible investor universe was modified to include mutual funds and workers.

b. Second phase from 1997 to 1999: The main highlight of disinvestment policy announced during this period is setting up of disinvestment commission for advertising on disinvestment related matters so as to implement decision to disinvest in a transparent manner.

c. Third phase 2000 onwards: During this period, the government classified, public sector enterprises into strategic and non-strategic for the purpose of disinvestments. This happened for the first. time in the history of disinvestment in India.

The following year wise strategic aims of disinvestment show different policies and reforms of disinvestment in India.

1991 Interim budget, Government announced 20% disinvestment in selected PSUs.

Their shares were sold to Mutual funds and financial institutions (UTI, EPFO, LIC etc.)

1992 Government decides to sells shares to FIIs, PSU employees and banks

1993 Rangarajan Committee suggests:

49% disinvestment in PSUs reserved for public sector

74% disinvestment in all other PSUs Government did not implement.

1996 Disinvestment commission under GV Ramakrishna. It was a non-statutory, advisory body (similar to UPA's NAC).

1998-2000 Vajpayee Government classifies PSUs into two parts

(i) Strategic: arms-ammunition, railway, nuke energy etc. here no disinvestment

(ii) Non-strategic: those not in above category. Here there is disinvestment in a phased manner. Hindustan Zinc, BALCO, Maruti Disinvestment taken up.

To implement above policy, Department of disinvestment setup under Finance ministry. (First there was disinvestment ministry, then department not going into all ball by ball commentary)

2004 UPA comes into power, Common Minimum program (CMP) updates disinvestment policy

(i) Sick PSUs will be revived

(ii) No disinvestment in profit making PSUs.

2005 Whatever Money Government earns from selling its PSU shares- it'll go to National investment fund (NIF).

Disinvestment remains stagnant because Left allies of the UPA Government stonewall everything.

2009 UPA-2 without left parties. Government resumes disinvestment process.

All PSUs can be disinvested, but upper limit 49%.

Disinvestment Method: only public offer.

2013-14 Oil ministry, mining ministry, trade unions opposed the move, files were delayed.

Lukewarm response from investors because share market was down due to internal & external factors.

2014 Modi cabinet approves disinvestment in NHPC, Coal India, ONGC

6 EPICFAIL PSUs will be closed down.

5 loss making but viable PSUs will be revived.

III. PERFORMANCE AND PROBLEMS—A CRITICAL EVALUATION

The policy of Government of India's on disinvestment has evolved over a period starting from 1991-92 when it was decided to disinvest up to 20 per cent of government equity in select public sector enterprises. In pursuance of announcement of disinvestment policy in the year 1991-92, the Government decided to (a) offer randomly structured portfolios of shares each with a reserve price based on complex valuation procedure; and (b) off-load the shares to institutional investors as a buffer between the Government and shareholders. This section evaluates the impact of disinvestment in India from 1991 to recent years.

Indian disinvestment scenario is full of problems and hurdles which have effectively diminished the rate of disinvestment. Beginning from the 1991-92 round of disinvestment, government equity disinvestment has been completed in 40 central PSUs upto March 2000. In this process, a total amount of Rs. 18,68 crores has been realized. Table 1 shows the target receipts, actual receipts and the methodology adopted for success of disinvestment in India since 1991.

Table 1: Disinvestment—Target Receipts, Actual Receipts and Methodology

Year	No. of PSEs in which equity sold	Target receipts for the year (Rs. in Billion)	Actual receipts (Rs. in Billion)	Methodology

1991-92	47 (31 in one tranche and 16 in other)	2500	3038	Minority shares sold by auction method in bundles of “very good”, “good”, and “average” companies.
1992-93	35 (in 3 tranches)	2500	1913	Bundling of shares abandoned. Shares sold separately for each company by auction method.
1993-94	--	3500	210	Equity of 7 companies sold by open auction but proceeds received in 94-95.
1994-95	13	4000	4843	Sale through auction method, in which NRIs and other persons legally permitted to buy, hold or sell equity, allowed to participate.
1995-96	05	7000	362	Equities of 4 companies auctioned and Government piggy-backed in the IDBI fixed price offering for the fifth company.
1996-97	01	5000	380	GDR (VSNL) in international market.
1997-98	01	4800	902	GDR (MTNL) in international market.
1998-99	05	5000	5371	GDR (VSNL)/Domestic offerings with the participation of FIIs (CONCOR, GAIL). Cross purchases by 3 oil sector companies, i.e. GAIL, ONGC and IOC.
1999-00	03	10000	1829	GDR (GAIL) in international market and MFIL's strategic sale, VSNL domestic issue.
2010-11	03	10000	1868	BALCO, KRL (CRL) and MRL through strategic sale/acquisition and LJMe.
2012-13	10	12000	5640	CMC, HTL, VSNL, IBP, PPL, Jessop and Co. through strategic sale acquisition.
2016-17	06	21000	15004	HZL, IPCL through strategic sale, MUL through rights issue.
Total	48*	87300	30653	

* Total number of companies in which disinvestment has taken place so far.
# Figures inclusive of amount expected to be realized, control premium, dividend/dividend tax and transfer of surplus cash reserves prior to disinvestment, etc.
Source: Ministry of Disinvestment, Government of India, 2017

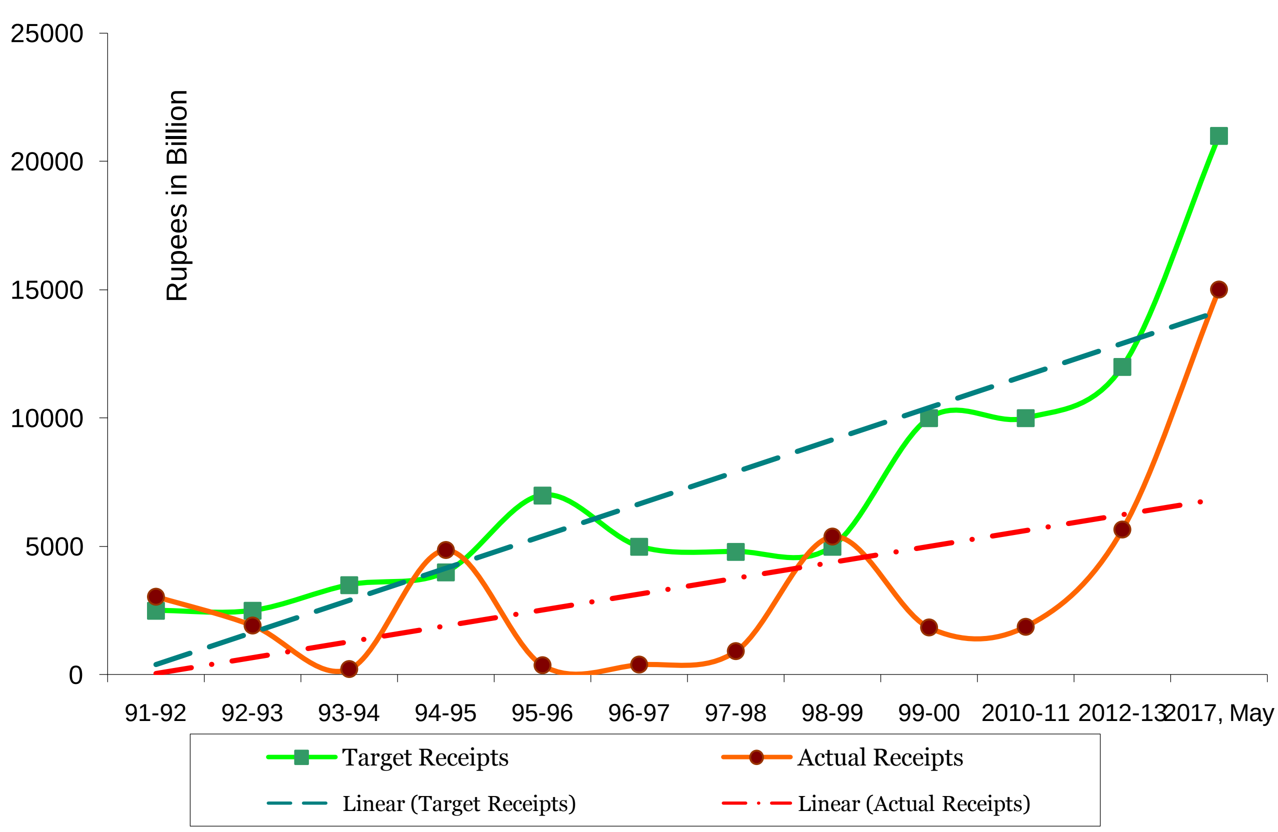

Chart 1: Disinvestment—Target Receipts and Actual Receipts

Table 1 (Chart 1 with trend lines) indicates the actual disinvestments from 1991-92 to 2017. The table 1 gives the information about the targeted amount of disinvestment, the actual receipts from disinvestment and the methods followed for disinvestment from 1991-92 to 2017. The Chart 1 provides the information of disinvestment in India with trend lines of both target and actual receipts.

2000-01 Onwards: Disinvestment Policy

The policy on disinvestment has evolved considerably through President's address to Joint Sessions of Parliament and statement of the Finance Minister's in their Budget Speeches.

The salient features of the Policy are:

(a) Public Sector Undertakings are the wealth of the Nation and to ensure this wealth rests in the hands of the people, promote public ownership of CPSEs
(b) While pursuing disinvestment through minority stake sale in listed CPSEs, the Government will retain majority shareholding, i.e. at least 51 per cent of the shareholding and management control of the Public Sector Undertakings; Strategic disinvestment by way of sale of substantial portion of Government shareholding in identified CPSEs upto 50 per cent or more, along with transfer of management control

Approaches of Disinvestment

(a) Disinvestment Through Minority Stake Sale: On 5th November 2009, Government approved the following action plan for disinvestment in profit making government companies;

- Already listed profitable CPSEs (not meeting mandatory shareholding of 10%) are to be made compliant by 'Offer for Sale' by Government or by the CPSEs through issue of fresh shares or a combination of both
- Unlisted CPSEs with no accumulated losses and having earned net profit in three preceding consecutive years are to be listed
- Follow-on public offers would be considered taking into consideration the needs for capital investment of CPSE, on a case by case basis, and Government could simultaneously or independently offer a portion of its equity shareholding
- All cases of disinvestment are to be decided on a case by case basis
- The Department of investment is to identify CPSEs in consultation with respective administrative Ministries and submit proposal to Government in cases requiring Offer for Sale of Government equity

(b) Strategic Disinvestment: To be undertaken through a consultation process among different Ministries/Departments, including NITI Aayog

- NITI Aayog to identify CPSEs for strategic disinvestment and advice on the mode of sale, percentage of shares to be sold of the CPSE and method for valuation of the CPSE.
- The Core Group of Secretaries on Disinvestment (CGD) to consider the recommendations of NITI Aayog to facilitate a decision by the Cabinet Committee on Economic Affairs (CCEA) on strategic disinvestment and to supervise/monitor the process of implementation.

(c) Comprehensive management of GOI's investment in CPSEs: The Government recognizes its investment in CPSEs as an important asset for accelerating economic growth and is committed to the efficient use of these resources to achieve optimum return.

- The Government will achieve these objectives by adopting a comprehensive approach for addressing critical inter-linked issues such as leveraging of assets to attract fresh investment, capital restructuring, financial restructuring, etc.
- Different options for optimal utilization of Government's investment in CPSEs will be assessed to adopt suitable investment management strategies to improve investors' confidence in the CPSEs and support their market capitalization which is essential for raising fresh investment from the capital market for their expansion and growth
- Efficient management of investment in CPSEs shall be ensured through rationalization of decision making process for all related issues and seamless inter-departmental coordination in the matter.

The disinvestment process adopted by the government for the strategic sale is given in Table 2.

Table 2: Disinvestment in India, 2017-18

CPSEs	% of GOIs Shares Disinvested	Methods of Disinvestment	Receipts	GOIs Shareholding Post-disinvestment
HCL	.07	Employees OFS	3.73	82.88%
NALCO	0.2125	OFS	1191.73	65.38.%
HUDCO	10.194	IPO	1207.35	89.87%
OIL	5.6	Buyback	1135.26	66.13%
RCFL	5	OFS	205.15	75%
NFL	15	OFS	530.72	74.71%
HCL	6.83	OFS	404.71	76.05%
CSL	25	IPO (Piggy Back)	470.01	75%
EIL	6.64	Buyback	657.81	54.17%
NTPC	6.65	OFC	9118.32	63.09%
BEL	0.25	Employees OFS	79.51	67.94%
Total Sum			15004.30	

Highlights of Progress

- Total disinvestment proceeds during the Current Financial Year 2017-18 is Rs. 19,157.95 crore (as on 20th September, 2017)
- The CPSE with the highest market capitalization is Indian Oil Corp.Ltd. at Rs. 2,20,433.81 crore (BSE) and Rs. 2,20,798.00 crore (NSE) (as on 31st August, 2017)
- CPSEs constitute 10.82% and 10.92% of the total market capitalization of companies listed at BSE and NSE respectively (as on 31st August, 2017)
- VSNL was the first CPSE to be divested by way of a Public Offer in 1999-00
- ONGC Public Offer in 2003-04 has been the largest CPSE FPO, raising Rs. 10,542 crore
- Coal India Public Offer in 2014-15 has been the largest CPSE OFS, raising Rs. 22,557.63 crore
- The maximum number of applications received in a PSU IPO/FPO since 2003-04 was in CIL (15.96 lakhs)
- Total disinvestments proceeds during the Financial Year 2016-17 was Rs. 46,246.58 crore.

IV. PROBLEMS OF DISINVESTMENT POLICY IN INDIA

The policy-makers in India do not at anytime appreciate the issue relating to disinvestment. As per international exercise on disinvestments, it is proceeded by appointment of qualified consultant to advice on the entire process of disinvestment and who also helps in the implementation. The disinvestment process still seems to be in complete disarray. To some extent, political factors, labour unions, state governments, bureaucrats and vested interests among competitors have stunted the process. The elements of transparency and maximizing the price have been missing throughout. Considering all these facts, the following are the important areas where the disinvestment problem persists.

1. Political Issues: Political Interference, Unnecessary criticism by opposition, difference between States and Central Government policies and opinions. Inter-ministerial conflict and delay in the process were characteristics of the execution of disinvestment policy in India.
2. Incompetency: Incompetency of those involved in disinvestment process, ignorance of technicalities like claw back provision, restructuring, etc. on part of policy-makers.
3. Valuation Problem: Lack of transparency in valuation, Faulty method of Valuation, Perception of under realization.
4. Regulatory Issues: Multiplicity of authorities at Centre and State level, feasibility and implication of transferring a monopolistic business to private sector, transferability of permits, licenses, leases to private sector entity, lack of adequate powers to authorities such as disinvestment commission etc.
5. Database: Disinvestment process lacks database. Database creation is essential for disinvestment. Such database should cover information about the industries and the functioning in India and it should also contain valuation for a company which is proposed to be disinvested. Non-availability of basic records, lack of availability of data regarding function and valuation of PEs are best examples.

All this and more problems created simply because of lack of transparency, proper policy and political issues involved in the deal. The poor outcome of the disinvestment policy particularly in the recent years is mainly due to lack of domestic capital, marginal interest of foreign capital and sharp differences between federal government and state governments and also between ruling parties and opposition parties including trade unions. The following table shows the Indian and Global Disinvestment Scenario.

V. INDIAN DISINVESTMENT ANALYSIS IN VIEW OF GLOBAL EXPERIENCE

For proper and comprehensive analysis of Indian disinvestment scenario it is necessary to evaluate it from global point of view which provides logical base for its evaluation as a whole. A critical analysis of the disinvestment exercise points to lack of clarity about the goal of disinvestment. In most of the countries like UK, Singapore and Malaysia, etc. the Governments have drawn very comprehensive framework of disinvestment. They have divided their disinvestment goals and objectives in short-run and long-run signposts. These programmes have had a tremendous impact on growth of capital market. Table 3 shows Indian v/s Global Disinvestment Scenario i.e. how India's disinvestment process is different from the rest of the world.

Table 3: Indian V/s Global Disinvestment Scenario

Characteristics	Indian	Global
1. Government Interference	Yes	No
2. Balanced Portfolio	No	Yes
3. Enterprises Restructuring	No	Yes
4. Compulsory Compilation of Recommendation	No	Yes
5. Comprehensive	No	Yes
6. Professionalism	No	Yes
7. Worker's Welfare given due consideration	No	Yes

Besides all the problems mentioned above, there is also a problem of determining right value. The determination of reserve price, realization of proceeds, particularly in business that have significant physical assets is a major issue in disinvestment in India. Beside this various regulatory issues such as transferability of permits, licenses, leases to private sector enterprises, etc. are also creating a major blockage to smoothen disinvestment process in India.

Suggestions for Improvement

In India, neither the calendar of disinvestment is drawn up nor very seriously adhered to. Time frame for disinvestment is uncertain. In other countries, disinvestment programme of PSEs has taken the form of physical, organizational, financial and manpower restructuring. India has missed the comprehensive understanding of the approach resorting to mostly financial restructuring which could not produce the desired results. India has fallen prey to the short-term objectives of raising revenues, leading to partial realization of benefits. Therefore, our disinvestment programme should be exercised to achieve the long-term objectives of enhancing competition, promoting optimum allocation of resources, etc.

India has preferred ownership disinvestment, resulting in minimal benefits. Again, even in the ownership realm, the Indian model of disinvestment has placed its complete reliance upon partial privatization. Regulation has been considered the key to the successful disinvestment. Barring the setting-up of the Central Electricity Regulatory Authority, State Electricity Regulatory Authority and the recently set-up Insurance Regulatory and Development Authority, the Indian scenario does not inspire any confidence in this regard. The absence of the much-desired regulatory framework has adversely affected competition, quality and delivery.

The Future of Disinvestment in India

Based on the Indian framework and experience of disinvestment presented earlier, following suggestions can be given in brief to ensure the disinvestment exercise successful:

- A separate enactment should be formulated to carryon the disinvestment exercise.
- An independent implementing machinery should be created for disinvestment.
- Full transparency should be ensured in the disinvestment process.
- The techniques selected for disinvestment should be enterprise specific.
- Regulation should precede disinvestment and the regulatory mechanism should have enough teeth.
- Restructure and revive potentially viable PSUs.
- Fully protect the interests of workers.

Ultimately, public awareness, employee's satisfaction, transparency of transactions, consultation with respective states, fair valuation of assets, using the proceeds of disinvestment for infrastructure development and modernization, and fair regulation will determine the success or failure of the disinvestment process. But as pointed out in preceding paragraphs government intervention, political vendetta, lack of clear policies and transparency as a whole has contributed towards the miserable performance of disinvestment process.

CONCLUSION

Disinvestment is the need of hour and it should be done more vigorously and effectively. It enables us to achieve the twin purpose of making PEs more competitive and finding funds to meet a fiscal deficit. However, government needs to reconsider its strategy of disinvestment which has been flawed on number of accounts. What is needed is to learn useful lessons from international experiences to convert the bleak picture presented by Indian disinvestment scenario into transparent and prosperous one. The Government should make its best efforts to make the disinvestment process transparent and should introduce concept of corporate governance in PEs. Further, necessary steps should be taken to create and sustain competitive capital market and to carry out necessary legal reforms

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