RESEARCH PAPER | Management | Volume : 3 | Issue : 8 | Aug 2013 | ISSN - 2249-555X

# Disinvestment Policy in India: Progress and Challenges

KEYWORDS: Disinvestment, Progress, Objectives and Challenges

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**ABSTRACT** *In the nineties, India's budgeting, fiscal deficits, and balance of payments problems kick started the government's urge to unlock the huge investments chained in the state owned enterprises (SOEs). The major thrust for Disinvestment Policy in India came through the Industrial Policy Statement 1991.The policy stated that the government would disinvest part of their equities in selected PSEs. However it did not stake any cap or limit on the extent of disinvestment. It also did not restrict disinvestment to any class of investors. The main objective was to improve overall performance of the PSEs. In eighties the model of privatization/divestment was initiated by Margaret Thatcher in UK and implemented by other countries including Germany (Unified), and other socialist countries. The Four Ps of disinvestment are Policy, Promise, Prognosis and Performance. In recent past, we have been witnessing a lot of debate on the disinvestments scenario suggesting dynamic movement.*

**Introduction**
The founding fathers of our republic used the public sector as an essential and vibrant element in the building-up of India's economy. The founding father of PSEs, Jawaharlal Nehru called the public enterprises set-up in various parts of the country as temples of modern India. India was not alone in ascribing an important role to the public sector. Many in the developed countries, who saw the devastation caused by inefficient and myopic managements of private sector enterprises, voted strongly for a growing public sector in U.K., France, Germany and even in U.S.A. The objective of accelerating the pace of economic development and the political ideology led to rapid growth of the state-owned enterprises sector in India.[3]

The public sector presence is predominant in public utilities and infrastructure. Railways, post & telegraph, ports, airports and power are dominated by CPSEs or department-owned enterprises. In telecom, the public sector continues to be dominant in the provision of fixed line telephone services, while private licencees are operating in some urban areas. Mobile services are predominantly private, particularly in urban areas, while inter-state and international linking services are significantly privately managed and owned.[4]

Public enterprise policy patterned on the Nehru-Mahalanobis mode has been experiencing drastic changes since July 24, 1991. The new policy announced as a constituent of the New Industrial Policy, 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 emerge as the most favoured reform by the government.[5]

The aims of disinvestment policy are i). raising of resources to meet fiscal deficit ii). Encouraging wider public participation including that of workers iii). Penetrating market discipline within public enterprises and iv). Improving performance.

The premise accepted by most of the high-ups in the top echelon of the Central Government is that the PSUs which were once created for "Public Interest" should gradually be disinvested in the "Public Interest" only. The logic and rationale behind such disinvestment policy are therefore, according to them, now stand well defined and transparent. It is for that reason, they feel, public exchequer in lieu of funding the PSUs should better be utilized for basic education, primary health, family welfare etc. of the country for which Government has at present hardly any surplus to allocate. After all it is inapt and ridiculous for the Government to become industrialist, trader or businessman instead of becoming a Government itself. Having aforesaid socio-economic dimension in the back-drop the Central Government likes to go by popular maxim "your business is your business and my business is mine" and wants to disassociate itself with the PSUs through disinvestment policy in a phased manner.[6]

**Evolution of the Disinvestment Policy**
The benefits of partial disinvestment of equity were envisaged for the first time by the Estimates Committee of the first Lok Sabha in its 16th report entitled Nationalized Industrial Undertakings, as early as 1955. The committee recommended that at lest 25% of the share capital of government companies should be available for subscription by the public, and the government could fix a ceiling for individual holdings as well as on the dividends to be declared by those companies. The government which was in no mood to dilute its stake in PEs, argued that the private investor will not be interested in investing in PEs, and that the committee's recommendation would have to be seen in the light of paras 7-9 of the Industrial Policy Resolution of 1956.[7]

The committee did not agree with this reply and remarked that the Industrial Policy Resolution did not bar public participation, as even for Schedule 'A' industries, which were to be the exclusive responsibility of the state, the possibility of the state securing private cooperation in establishing new units, where national interest so required, was not precluded. The 13. committee added that public participation would help in efficient functioning of PEs and it would also evoke the enthusiasm of the public for participation in the national development. It further argued that PEs themselves would function effectively under the vigil of a body of shareholders, who would in their own interest keep a watchful eye on the working of the undertaking. But the government did not relent.

About the same time, the Krishna Menon Committee recommended 25% equity participation in PEs by the public at large because: (i) it was a method of financing the capital, (ii) it would help in mopping up of additional earnings of lower income groups and was thus an anti-inflationary measure, and (iii) it enabled people to participate in profit of PEs or to share their burden. But this recommendation was also ignored by the government.

In October 1960, a committee headed by the then secretary of the Department of Company Affairs recommended to the Planning Commission that 25% of PE equity be disinvested to the public. The Chandrashekar government took the bold decision on disinvestment on 4th March, 1991. Its finance minister, Mr. Yashwant Sinha presenting the budget for 1991-92[8] stated: The Congress government's Industrial Policy Statement of 25th July, 1991 gave the reasons for equity disinvestment. It made no mention about the extent of disinvestment.[9]

On 12th October, 1991 the finance minister also announced at the IMF World Bank meeting his government's decision to raise Rs. 2,500 crores through PE disinvestment in two installments of Rs. 1,250 crores each by 31st December and end of February, 1992. In pursuance to this decision, the government had to hurriedly complete the first round of disinvestment before the end of fiscal 1991-92.[10]

The Statement of Industrial Policy of July 24, 1991 stated that in order to raise resources and encourage wider public participation, a part of the government's shareholding in the public sector would be offered to mutual funds, financial institutions, general public and workers. After 1996, sale through the GDR route was also initiated and MTNL (1997-98), VSNL (1996-97 and 1998-99) and GAIL (1999-2000) all used the opportunity to access the GDR market.[11]

**Process of Disinvestment – Guidelines**

As of today the Government's decision to go for disinvestment of its PSUs has created a phenomenal impact over the economy of the country. This is an endeavour by the Central Government to govern the economy through applied approach thereby bridging the gap of deficit financing and gradually do away with control and regulatory measures. Since the process of disinvestment involves a number of complex procedures, it is absolutely necessary to have standard guidelines for proper accomplishment of various activities at different levels. The council of ICAI is perhaps the most appropriate authority in the country to evolve just and equitable guidelines and Accounting Standards for the various stages of disinvestment to serve the purpose best.

The initial steps involved in mooting a proposal for disinvestment, which may emerge from the policy of the Government of India or a proposal made by the Disinvestment Commission and clearance of the same by the Cabinet Committee of Disinvestment (CCD) incorporate procedural aspects of the Government. Outsiders get involved in the picture when Advisor is appointed generally through paper advertisements. "Advisor" does not stand to signify any singular entity rather reputed and established firms of professionals, Consultants, Banks, NBFCs etc. having national and international background may qualify for the task. So far the question of a firm of Chartered Accountants and consultants is concerned ICAI has enough justifiable prudence and wisdom to issue guidelines on important and "the must" areas to be covered by the Advisor while making due diligence of the PSU concerned. The same set of guidelines may also apply when a prospective bidder would undertake due diligence before bidding for the PSU. PSUs as we all know, are Government Companies under the Companies Act, 1956, since the Government, State or Central, holds more than 51% of its equity. Companies Act however, it is interesting to note, does not define a PSU nor the same has been defined under any other Act. When shareholding of the Government in a Government Company goes below 51% the Company loses its entity as a Government Company. But even then will it be called a PSU? Such type of relevant questions in PSU disinvestment should draw the attention of ICAI at the time of framing the prospective and justified guidelines to cover these areas.[12]

It is imperative that both the bidding firm, if it is a company, and the PSU Itself have to comply the requirements of various Accounting Standards already in vogue. But in many of the PSUs, as is very often experienced, ascertainment of figures with exatitude so far the liabilities are concerned are hardly made thereby leaving a vulnerable scope for hidden liability. Barring a few most of the PSUs have huge landed property on which there will always be an "eagle eye" of the pseudo bidders or "fly-by-night operators", who instead of carrying out the business will only be interested in asset stripping of the newly acquired PSU. Further, closing of branches or sales offices situated in the posh business localities of the various Metros with the plea of cost control is an area of orphic nature which should entice the vigilant eyes of the auditors for proper dissection of each case. Since the possibilities of transaction taking an untoward, undesirable and wanton turn benefiting some interested quarters rather than the PSU itself cannot be ruled out. Therefore to provide proper safeguard to the Government, shareholders, employees of the PSU and to the nation at large, stock of the situation should be taken without further delay and befitting guidelines and standards be evolved. Then only we shall be able to fulfill our professional commitment to the society.[13]

**Disinvestment and Privatization**

Disinvestment was initiated by selling undisclosed bundles of equity shares of selected central PSEs to public investment institutions (like the UTI), which were free to dispose off these shares in the booming secondary stock market. The process however came to an abrupt halt when the market collapsed in the aftermath of Harshad Mehta led scam, as the asking prices plummeted below the reserve prices. (Though disinvestment was not part of the scandal, the process got some what discredited as some officials associated with the policy reforms were found have had an association with Harshad Mehta).[14]

The change of government at the Centre in 1996 led to some rethinking about the policy, but not a reversal. A Disinvestment Commission was constituted to advise the government on whether to disinvest in a particular enterprise, its modalities and the utilization of the proceeds. The commission, among other things, recommended:

- Restructuring and reorganization of PSEs before disinvestment,
- Strengthening of the well-functioning enterprises, and
- To utilize the disinvestment proceeds to create a fund for restructuring of PSEs.

In response to the public debate, and to the commission's recommendations, some large and well-functioning PSEs were declared "jewels" (Navaratnas) in the government's crown, and were granted greater managerial and financial autonomy. However, disinvestment did not pick up as the share prices remained subdued because of the scandals that rocked the financial markets.10 But, by the turn of the decade, there was some improvement mainly in response to the stock boom engineered by Ketan Parikh. Apparently some PSEs stocks were part of the scandal, which this time also involved the UTI. (It is perhaps worth reminding ourselves that the 1990s witnessed a series of frauds in the financial sector that seriously dented the credibility of the stock market, which is yet to recover in terms of participation of domestic "small" investors. After the Harshad Mehta scam, there was, MS Shoe scam, collapse of NBFCs, vanishing companies scam, teakwood plantation scam, collapse of CRB group of financial companies, collapse of housing bubble in 1996, and finally the Ketan Parikh scam in 2000).

The new government that came to power in 1998 preferred to sell large chunks of equity in selected enterprises to "strategic" partners – a euphemism for transfer of managerial control to private enterprises. A separate ministry was created to speed up the process, as it was widely believed that

Volume : 3 | Issue : 8 | Aug 2013 | ISSN - 2249-555X

the operating ministries are often reluctant to part with PSEs for disinvestments as it means loss of power for the concerned ministers and civil servants. The sales were organized through auctions or by inviting bids, bypassing the stock market (which continued to be sluggish), justified on the grounds of better price realisation. Notwithstanding the serious discussion on the utilization of disinvestment proceeds, they continued to be used only to bridge the fiscal deficit.[15]

Strategic sale in many countries have been controversial as it is said to give rise to a lot of corruption, discrediting the policy process. Aware of such pitfalls, efforts were made to be transparent in all the stages of the process: selection of consultants to advice on the sale, invitation of bids, opening of tenders and so on. Between 1999 and 2003, much greater quantum of public assets were sold in this manner, compared to the earlier process, though the realized amounts were consistently less than the targets – except in 2003.

Nonetheless, there are series of allegations of corruption and malpractice in many of these deals that have been widely discussed in the press and the parliament. Instances of under pricing of assets, favouring preferred buyers, non-compliance of agreement with respect to employment and retrenchment, and many incomplete contracts with respect to sale of land, and assets have been widely reported.

Thus, during the last 13 years Rs. 29,520 crores were realized by sale of equity in selected central government PSEs, (in some cases) relinquishing managerial control as well. This formed less than one per cent of central government's cumulative fiscal deficit in this period.

Amid disinvestment and privatization, some new PSEs are also created. For instance, many departmental activities were being corporatized (setting up of BSNL for instance) with a view to disinvestment. New PSEs are also formed to take up newer activities like road development corporations.

**Disinvestment : Scenario of Indian Mindset**

The Indian approach to disinvestments seems to have gone wrong being positioned in the middle between the doctrinarian extreme on the one end and the laissez faire extreme on the other. The country seems to have lost both the opportunity and the direction, and the pace is poor, lethargic, and lacklustre. While all political parties and economists believe in the principle of divestments/privatization, they devise escape routes for non-implementation by taking recourse to statements such as: "We agree in principle but differ in the details;" "First bring in a strategic partner and then divest;" "First increase the equity base through a public offer and then divest;" "It is videshi, swadeshi;" etc.[16]

The industry and business express their doubts about raising such huge funds to buy out and acquire PSUs. The foreign investors are critical of the entire process and are often seen withdrawing from the bidding process. In essence, there is something seriously wrong in India's approach to disinvestment and implementation.

**Conclusion**

The public sector enterprises' contribution to national development is widely acknowledged, their poor financial return has been a matter of deep and enduring concern, especially since the mid-1980s when, for the first time, the central government's current revenues were found inadequate to meet its current expenditure. Though firm and industry level studies of PSEs have often highlighted gross inefficiencies and poor profitability, many of them have also suggested their unquantifiable (or difficult to quantify) non-economic benefits. However, macroeconomic discourse in India has largely focused on the "crowding-in" effects of public investment, and the need for institutional structures to insulate the PSEs from political and bureaucratic interference to improve their financial returns. Deeper analyses have sought to offer political economic explanations for continuation of such a state of affairs.

The following five-point agenda may be useful for policy-makers.

- Trust the homegrown expert: If we look at the domains of cutting edge expertise, the lead players whose initiatives the advanced countries have trusted are products of our own institutions.
- Place administrative control in the hands of the Finance Minister: This would enable him to complete the disinvestment process focusing on FDI which could be deposited in the Disinvestments Fund.
- Hand over companies that are a burden on the government to the employees: This could be done on a token share price of one paisa per share. They may turn the company around or resell it for scrap or close down the outfit.
- Do not involve a PSU/SOE in the bidding process: A PSU/SOE should not be allowed to invest or control management interest in a PSU/SOE disinvestment candidate. This in effect is asset stripping by the GOI and a transfer payment (one government pocket to another pocket) from the bidder PSU to the government treasury.
- Manage revivals: Any revivals must be professionally managed on a lease basis.

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