PRIVATISATION OF PUBLIC SECTOR UNDERTAKINGS – OPPORTUNITIES AND CHALLENGES

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Introduction

The world at large is evolving and is demanding the need for change for all of us by making us proactive instead of being of a reactive person. Over the past decade, one of the most popular and trending topics around us has been **Privatisation of the Public Sector Undertakings (hereinafter referred to as PSUs)**.

What are the Public Sector Undertakings?

- The government-owned companies are known as Public Sector Undertakings (PSUs).
- In a PSU majority i.e. 51% or more of the paid-up capital is owned by the central government/any state government/partly by the central governments and partly by one or more state governments.

What are the types of public sector undertakings?

- Public Sector Undertakings are classified as Public Sector Enterprises (PSEs), Central Public Sector Enterprises (CPSEs), and Public Sector Banks (PSBs).

The term privatisation mainly refers to the removal of government/public sector intervention from the business of the entity and providing an open-ended way out for the entity and its management to think about the future prospects for the growth of enterprises/organization/company. **As our Honourable Prime Minister Narendra Modi says, Privatization is the need of the hour and the Government has no business to be in business**. The aim of India's economy touching the **$ 5 Trillion-mark,** privatization would play a major role, as the enterprises which have the potential to steer their work force and show a multi-folded growth would get the opportunities to forecast themselves into broader picture. Privatisation may look and sound easier but the reality is a bit different. There are numerous opinions of the people of the nation over the Privatisation of PSUs, few resulting into Opportunities and few others into Challenges. Developing countries have been quick to jump on the privatization bandwagon, sometimes as a matter of political and economic ideology, other times simply to raise revenue. In our daily routine itself, we all can see both aspects of the PSUs, i.e. the opportunities and the challenges it may face once it gets privatised. Ranging it from:

1. The Job losses people may face to the betterment of the services countrymen may receive,
2. The pollutants arising in the locality (due to aggressive business tactics) to the infrastructural growth of the surrounding due to betterment in the business environment,
3. There are concerns about crony capitalism also,

   & Many more which we shall discuss ahead in detail…

The desire to involve the private sector in the management and provision of port infrastructure and services is prompted by the recognition that government regulations and processes are not always conducive to efficient operations of commercial activities and by recognition of the private sector's relative strength in this field. Also, in recognizing that investment sources outside government must be tapped in the provision of such infrastructure and services involvement of the private sector provides the opportunity to share risks and, in times of rapidly changing economic environment to respond quickly to market/demands and opportunities.

What is the need to privatize the PSUs?

- The private sector has come a long way and acquired the will and capacity to compete at the world stage. It no longer needs the government to take care of non-profit-making industries. Rather it is seeing opportunities in areas like railways too through investments in Mass Rapid Transit System.
- There are many advantages of privatization that could be complementary to the developmental targets.
- Privatization raises government finances that can be spent in social sectors.
- It creates money for restructuring and improvements necessary for PSUs.
- It brings in professional management to the mismanaged PSUs. It increases the profitability of the firms.
- Privatization brings in more investment including Foreign Direct investment.
- It also helps in up-gradation in technology, skills, and operational efficiency.
- It reduces the public debt that is rising to unsustainable proportions.
- It also releases resources such as large government manpower currently locked up in managing PSUs to be redeployed in priority areas.

Source of the Idea

For decades prior to the 1980s, governments around the world increased the scope and magnitude of their activities, taking on a variety of tasks that the private sector previously had performed. In the United States, the federal government-built highways and dams, conducted research, increased its regulatory authority across an expanding horizon of activities, and gave money to state and local governments to support functions ranging from education to road building. In Western Europe and Latin America, governments nationalized companies, whole industries, banks, and health care systems, and in Eastern Europe, communist regimes strove to eliminate the private sector altogether. The concept of privatisation became popular in India during the liberalization policy introduced by the Indian Government in the year 1991. The liberalization policy came out to be a success for the growth of the country and the countrymen in terms of betterment of business and the business environment. India has a mixed economy in which both Private and Public Sectors exist especially in the areas of Banking, Telecom, Road Transport, Education, Healthcare, Manufacturing and Education. Many Business analysts and experts on Economy are of the view that privatization could speed up economic growth with the increase in competition. So, should India opt for privatization or continue with the current system, is a burning discussion topic in view of the various steps taken in different sectors. Whether the move will benefit the country or will not be feasible needs to be evaluated by discussing the Opportunities & Challenges of the Privatisation of the PSUs.

At independence, India adopted a mixed economy model. In this context, the Public Sector Enterprises (PSEs) were established on a socialistic pattern of development. Apart from that, there was a need to create adequate infrastructural facilities which served as the most important consideration leading to the expansion of the PSEs. However, due to the poor performance of several PSEs and the consequent huge fiscal deficits, the issue of privatisation has come to the forefront. Privatisation is ought to infuse efficiency by bringing PSEs to the competition in the market. The term ‘privatisation’ is used in different ways, ranging from ‘transition to private legal

forms’ to ‘partial or complete denationalization of assets.’ In India, privatisation is sought to be achieved through two measures: The disinvestment of the government’s equity in public sector

undertakings. Disinvestment: Selling off public sector equity to mutual funds, financial institutions
and the private sector. The opening up of hitherto closed areas to private participation. The current direction of privatisation of PSEs has been spelt out in a policy laid down by parliament in 2002. The policy stated that the main objective of disinvestment is to put national resources and assets to optimal use and in particular to unleash the productive potential in our public sector enterprises.

Brief structure for Privatisation and Nationalisation:

	Privatisation	**Nationalisation**
Ownership	Private Sector	Government
Incentives	Profit motive acts as incentive for owners and managers.	Workers may feel motivated if they feel company belongs to them.
Externalities	Private firm may ignore external costs (pollution).	Government can put social benefits above profit motive.
Efficiency	Incentives increase the productivity with new age ideas	Nationalised firms may find it difficult to sack surplus workers
Knowledge	Employment is based on skills and on merits	Political interference based on political motives

In India, there seems to be broadly three positions with respect to the privatisation of PSEs:

- One, PSEs should not be sold irrespective of its performance.
- Second, the market view i.e. the business is not the business of government.
- Third, the privatisation of profit-making PSEs is also debated.
  For example, Bharat Petroleum Corporation Limited (BPCL) which is making handsome profits, comes under this category.

Opportunities

The desire to involve the private sector in the management and provision of port infrastructure and services is prompted by the recognition that government regulations and processes are not always conductive to efficient operations of commercial activities and by recognition of the private sector's relative strength in this field. Also, in recognizing that investment sources outside government must be tapped in the provision of such infrastructure and services involvement of the private sector provides the opportunity to share risks and, in times of rapidly changing economic environment to respond quickly to market/demands and opportunities. The opportunities waiting for PSUs being privatised are:

1. **Save Taxpayers' Money**

   By applying a variety of privatization techniques to state services, infrastructure, facilities, enterprises, and land, comprehensive state privatization programs can reduce program costs. Over 100 studies have documented cost savings from contracting out services to the private sector. Cost savings vary but average between 20 and 40 percent, depending on the service. For some services like catering business of Indian Railways savings are often greater. Competitive bidding whenever possible and careful government oversight are crucial to sustained cost savings. States can also realize large one-time windfalls from the sale or lease of state infrastructure and facilities. Moreover, privatization can put an end to subsidies to previously government-run operations. Privatization also creates a steady stream of new tax revenues from private contractors and corporations who pay taxes and license fees, while state units do not.

2. **Increase efficiency and innovation**

   Private management can significantly lower operating costs through the use of more flexible personnel practices, job categories, streamlined operating procedures, and simplified procurement. Private ownership can stimulate innovation. Competition forces private firms to develop innovative, efficient methods for providing goods and services in order to keep costs down and keep contracts. These incentives, for the most part, do not exist in the public sector.

3. **Improved Maintenance**

   Private owners are strongly motivated to keep up maintenance in order to preserve the asset value of the investment in the facility. Improved maintenance helps in better production quality from the plant and machinery. Public owners often defer maintenance due to political considerations, increasing overall long-term costs.

4. **Optimum Utilisation of Scarce Resources**

   It has been observed that the public sector has failed in the optimal use of national resources. The private sector may succeed in the optimum use of resources by maintaining efficiency and reducing overhead costs and increase in use of scarce resources.

5. **Reduction in Political Interference**

   The process of privatization reduces political interferences in the public sector enterprises by giving more representation to the private sector in the management of Public Enterprises. The improvement of the regulation of the economy by reducing conflicts between the public sector's regulatory and commercial functions. Privatization liberates the economy from state control. Without government regulations dictating market progression, the market operates organically. Due to a lack of government interference, the market becomes more dynamic and follows integral economic values of demand and supply. Consumer response to a more dynamic and organically run market is greater and generates higher revenues. Privatization allows state officials to spend less time managing personnel and maintaining equipment, thus allowing more time to see that essential services are efficiently delivered.

6. **Better Customer Service**

   As private companies are profit-driven and function in a competitive market, their primary focus rests on efficient customer service. State-run companies lack this feature as they face no competition and are not financially motivated. Furthermore, customer service is enhanced in privatization due to the elimination of unnecessary bureaucratic hassle. A number of surveys have indicated that public officials believed service quality was better after privatization. In a survey of 89 municipalities conducted in 1980, for example, 63 percent of public officials responding reported better services as a result of contracting out.

7. **Increased competition**

   Often privatisation of state-owned monopolies occurs alongside deregulation – i.e. policies to allow more firms to enter the industry and increase the competitiveness of the market. It is this increase in competition that can be the greatest spur to improvements in efficiency. For example, there is now more competition in telecoms (after entrance of Jio in the market and disturbing all the competitors and creating new way of business) and distribution of gas and electricity. If competitive bidding is instituted for a service, service quality can improve even if the service is retained in-house. The reason is simple: "Competition induces in-house and private service providers to provide quality services in order to keep complaints down and keep the contract".

8. **Intrapreneurship Opportunities**

   Intrapreneurs are self-motivated, proactive, and action-oriented people who have leadership skills and think outside the box. Often in the state-owned enterprises these intrapreneur talents remain hidden and don't get the limelight they deserve. This intrapreneurs often brings innovative ideas which helps in creating the best outcome for the overall working of the organization.

9. **Streamline And Downsize Government**

   Privatization is one tool to make bureaucracies smaller and more manageable. Large private corporations often sell off assets that are underperforming or proving too difficult to manage efficiently. Under new owners and leaner management, such divisions often receive a new lease on life. Entrepreneurial governments can replicate this experience.

10. **Privatisation of profit-making PSUs**

    There are various PSUs who have the ability and the monopoly in their sector and still are not performing well (i.e. they are profit making but can grow more and help the economy grow more stronger, but due to political influences they don't provide results which they are capable of providing and hence privatising the same would give a boost to the workers and the staff of their organization to perform more productively. This will still bring in benefits of the efficient operation of the private sector through reduced costs. For example, Air India is marred with issues like poor punctuality, high staff-top lane ratio, high operating costs and overall customer indifference. These issues will now be rectified by the Tata Group acquiring back their old gem.

11. Increase Flexibility

Privatization gives state officials greater flexibility to meet program needs. Officials can replace the private firm if it isn't meeting contract standards, cut back on service, add to service during peak periods, or downsize as needed.

12. Reduce the financial and administrative burden on the public sector

Public management of a port or a system of ports on a day-to-day basis generates a considerable demand on governmental resources in terms of time and personnel for what is largely a commercial enterprise. Whilst this resource demand falls most heavily on directly concerned ministries and agencies (e.g. Transport) it can be shown that it frequently spills over to those peripherally involved (e.g. Treasury) organization and even to the Cabinet itself.

Challenges

This section addresses the issues, and the decisions which governments themselves must make prior to embarking upon a privatization process. They may vary from project to project.

The initial groundwork and clarification of objectives recommended herein should enable governmental sponsors of ports privatization to chart their course with greater clarity. This in turn should lead to a smoother, faster internal process. It should also attract a greater number of interested, qualified and eligible investors/operators; thereby, providing government with the widest range of choice and the best opportunity of achieving objectives.

1. **Problem of Price**

   The government usually want to sell the least profitable enterprises, those that the private sector is not willing to buy at a price acceptable to the government. There are many of the PSUs which are underrated and can fetch a hefty valuation as they usually are cash rich organisations. But the problem with it is, there plays a political game around the organization which affects the Working Capital cycle and makes it worse for them to perform more effectively.

2. **Natural Monopoly**

   A natural monopoly occurs when the most efficient number of firms in an industry is one. For example, tap water has very significant fixed costs. Therefore there is no scope for having competition amongst several firms. Therefore, in this case, privatisation would just create a private monopoly which might seek to set higher prices which exploit consumers. Therefore it is better to have a public monopoly rather than a private monopoly which can exploit the consumer.

3. **Public Interest**

   There are many industries which perform an important public service, e.g., health care, education and public transport. In these industries, the profit motive shouldn't be the primary objective of firms and the industry. For example, in the case of health care, it is feared privatising health care would mean a greater priority is given to profit rather than patient care. Also, in an industry like health care, arguably we don't need a profit motive to improve standards. When doctors treat patients, they are unlikely to try harder if they get a bonus.

4. **Short – termism of firms**

   As well as the government being motivated by short term pressures, this is something private firms may do as well. To please shareholders they may seek to increase short term profits and avoid investing in long term projects. For example, the UK is suffering from a lack of investment in new energy sources; the privatised companies are trying to make use of existing plants rather than invest in new ones.

5. **Concentration of Economic Power**

   The private sector emerges a monopoly and the concentration of economic power in the hands of few. The dominance of some business groups in terms of capital and assets is an economic and social problem. The private sector operates on the principle of maximization of the Monopoly profits. It is harmful to consumers and society as a whole. There are possibilities whereby two or more entities would come together in a particular sector and create a duopoly and then rig the prices of the items/services which only they are offering and so ultimately the people of the nation had to suffer because of high service cost.

6. **Increase in Unemployment rate**

   With modernization and digitalisation of the business era, most of the private entities are moving towards automation of services whereby there is less requirement of man power and so they do remove the workers/staff which are not required and the same manpower is replaced by the machinery which is resulting into job losses and the job losses affects the family member of the person who losses the job in all ways. With PSUs there is a job security whereas in private companies there is no such thing of job security because the moment the employee is not required by the organization he has to vacant his position and which results into unemployment.

7. **Stakeholder perspective**

   No investor would want to struggle navigating through cultural integration and low employee morale cauldron while focussing on critical business retention/expansion strategies necessitating periodic capital infusion. Stakeholders perspective is to earn profits either in the form of dividend or capital appreciation and while the company is a PSU, they deliver good return to their investors and hence it will be a key challenge for the new private firm who is either overtaking the same PSU or the new management that is running the PSU to make sure that they deliver the same form/kind of returns to their stakeholders in the forceable future as well. Being a private player, there is no certainty on the profit figures as there can be major capex happening which would eat over the reserves accumulated over the period of time by the entity being an PSU.

8. **Hardships faced by people**

   If government driven services will be provided by the private players then they may increase the price for the goods/services offered by them and the general public would have to suffer because of rise in the purchase price of the daily needs of living. Eg: If Railways will be privatised then the motive of the management team would be to earn profits which will not be acceptable by the general public as they have been habitual to travel in a very nominal cost throughout the life span and a sudden change in the price of the services would not attract more people to use the service and instead they will try to switch to other modes of transport and this would cause a major challenge for the management team to strive in the market with such a huge cost to be repaid.

Way forward

- While, disinvestment and privatization in loss-making assets is a common wisdom now, we must not forget that there are slippery slopes in this path.
- We must not get carried away and sell the PSUs for lesser prices than expected just for the sake of privatization.
- A proper judgment of the value of the PSU is necessary and Railways and BPCL are some of the sectors where the proper pricing is difficult to come up with as the potential for future growth is high as of now.
- There is an issue with how do we utilize the proceeds of disinvestment. Using it for bridging the revenue deficit and neglecting dire needs of modernization of existing strategic sectors and asset creation will be a huge misstep.
- To make the assumptions of cronyism go, the process of privatization must be fair and transparent with a level playing field to all players. A third-party evaluation of assets and a minimum number of bidders should be necessary pre-conditions to ahead with each sale.
- The after-privatization governance is also important and the private player that wins the bid must be made accountable so that the existing socio-economic functions of that asset must continue and they are not sacrificed for profit motives.
- The regulatory mechanism also needs to change if the all-around privatization takes shape. This is a critical process as we must balance the socio-economic needs with market requirements of freedom of operation.
- The new policy must take into account all these issues and come up with a fool-proof policy to regulate the Privatization and after.
- The government will focus more on privatization going forward in line with the public sector enterprises' (PSE) policy framed last year. This will create more jobs and have a broader impact on the economy, rather than just stake sales.
- A clear - cut policy on indigenisation and privatisation should be developed, there should be transparency in the privatisation policy and an improvement in the quality of governance in the country.
- Draw lessons from other countries rather than reinvent the wheel.

Facts

1. Disinvestment receipts constituted 0.95-4.68 per cent of the total receipts of the Centre during 2014-15 to 2020-21, according to data given by the minister in the House. While the proportion was the least at 0.95 per cent during 2020-21, it was the highest at 4.68 per cent during 2017-18, showed the data

2. The revised estimates (RE) for disinvestment receipts in 2020-21 was Rs 32,000 crore. As on March 31, 2021, the government has realised disinvestment receipts of Rs 32,845 crore, which is around 103 per cent of the RE in 2020-21.

3. As much as Rs 37,134 crore of the goods and services tax (GST) compensation was pending to states for 2020-21 and Rs 14,664 crore for the first half of the current fiscal year. This is after taking into account the amount released from the compensation fund and back-to-back loans, minister of state for finance Pankaj Chaudhary told the Lok Sabha.

4. Twenty years is a long time. That's what it took to execute the privatisation of Air India. The process was set in motion in year 2000, albeit the idea for selling it was first proposed in 1988, following the successful sell-off of British Airways and other national assets by the Margaret Thatcher government in the UK. "Air India was the Holy Grail of public sector privatisation. The sentiment in the government was, 'If we can success-fully privatise Air India, we can sell anything.' Now that it's done, it's up to them to leverage it," a market source told Business Today requesting anonymity. The sale of Air India is to fetch the government ₹18,000 crore, and would give the buyer, Tata group, ownership of Air India, its low-cost unit Air India Express, and a 50 per cent stake in the airline's ground and cargo handling subsidiary, Air India SATS Airport Services (AISATS).

5. The upcoming LIC IPO is fundamentally a big positive. LIC is a superb organization built over the past several years. A successful listing will give it a thrust to expand globally.

6. The Centre has broadened its privatisation policy to disallow public sector undertakings (PSUs) and cooperative societies from participating in the bidding for other state-owned firms. The Department of Investment and Public Asset Management (DIPAM) has also asked all government departments to inform PSUs and cooperative societies under their administrative control that they will not be permitted to participate in the privatisation process unless otherwise specified.

THEIR TIME HAS COME

These companies are likely to fetch good valuations if they are privatised on priority

**Consolidated revenue for the year ended March 2021*

Company	Revenue in ₹ crore*	Likely bidders
Steel Authority Of India Ltd (SAIL)	69,113.61	Vedanta, Tata Steel, Nippon Steel
Bharat Sanchar Nigam Ltd (BSNL)	17,452.11	Reliance Jio, Bharti Airtel
Container Corporation of India Ltd (CONCOR)	6,427.08	Adani, Allcargo Group, Gateway Distriparks
Shipping Corporation of India (SCI)	3,703.25	Reliance, Adani Shipping India, Great Eastern Shipping
BEML Ltd	3,556.64	L&T, Adani
Hindustan Copper Ltd	1,786.76	Vedanta
Mahanagar Telephone Nigam Ltd (MTNL)	1,387.71	Reliance Jio, Bharti Airtel

Source: *ACE Equity; industry*

Conclusion

The PSU privatization is a long-lagging process. This is thought to be a necessary pre-condition for growth and good governance of the existing PSUs. Amid the pandemic hit market conditions, it needs to be seen if the current drive fetches good results. At any cost, the poor of the country must not bear the cost of aspirations of the remaining middle and higher class. Any future policy must be aware of the tremendous role that PSUs played and still play. Problems at home, typically drying national coffers, and opportunities outside, especially globalization, plus social change, have made privatization popular with governments. While privatization can help ameliorate some of the pressing problems states face, such as providing revenue for a cash-strapped government, it is by no means a panacea for all the ills of the public sector or the wider society. However, privatization's success will, to large extent, depend on the quality of the political and economic environment within which it occurs and the approach adopted in implementing it. Although there is no one-size-fit-for-all approach to privatization, the key thing is to learn from the good and bad experiences of others, and to apply them to the exigencies of the local context in order to maximize the gains, while minimizing the costs, of privatization. That said, it should be borne in mind that there will always be winners and losers in any privatization policy. The key issue seems not to be whether or not to privatize but where, how, and how much to privatize, so as to distribute its benefits (and costs) equitably. This is where joint ventures and Public-private-partnerships (PPPs) seem to offer some hope to governments.

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