# MALAVIYA NATIONAL INSTITUTE OF TECHNOLOGY

# CHANGE IN ROLE OF PUBLIC SECTOR ENTERPRISES IN INDIA


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## INTRODUCTION

**Public sector Enterprises**

"Public enterprises are autonomous or semi-autonomous corporations and companies established, owned and controlled by the state and engaged in industrial and commercial activities."

The business units owned, managed and controlled by the central, state or local government are termed as public sector enterprises or public enterprises. These are also known as public sector undertakings.

A public sector enterprise may be defined as any commercial or industrial undertaking owned and managed by the government with a view to maximise social welfare and uphold the public interest.

Public enterprises consist of nationalised private sector enterprises, such as, banks, Life Insurance Corporation of India and the new enterprises set up by the government such as Hindustan Machine Tools (HMT), Gas Authority of India (GAIL), State Trading Corporation (STC) etc.

These are mainly divided into CPSEs,PSBs, and SLPEs.

Although investments in government undertakings are done by the government, they become financially independent. They are not dependent on the government for their day- to-day needs. These enterprises arrange and manage their own finances. An element of profitability is also considered while pricing their products. It has helped the enterprises to finance their growth themselves.

## OBJECTIVES OF PUBLIC SECTOR ENTERPRISES

Objectives of Public Sector may be divided into two parts:

(1) Economic Objectives

(2) Social Objectives

## Economic Objectives

- **Economic Development:** Public enterprises are established to accelerate the economic growth by setting up keys and basic industries like iron,steel, petroleum, power generation, chemicals, machine building etc. the expansion of capital goods industries leads to development of other industries.
- **Planned Growth:** Private sector neglects those industries which have long gestation period and low rate of returns , but Public Enterprises take steps to fill up these gaps by setting up industries which are less profitable but nationally important and create a plan so that they may grow.
- **Balance regional Development:** Public sectors are designed to facilitate the growth of backward region so as to reduce regional disparities in industrial growth.
- **Generation of surplus:** They are expected to generate and distribute surplus for financing five year plans and other schemes of public welfare.
- **Employment generation:** One of important objective of public sector reduce unemployment by creating employment opportunities.
- **Export promotion and Import substitution:** As we know capital formation is necessary to trade with foreign and for it we need foreign exchange reserves which can be obtained by increase in exports and reduction in imports.

## Social Objectives

- **Control Monopoly:** Sometimes monopoly of private sector is unbearable for public at this time, such as increase in prices of product is main thing, in this case public sector can break their monopoly and control the situation.
- **Equitable Distribution of Wealth:** Public Enterprises are expected to reduce disparities in distribution of income and wealth.
- **Provision of Essential goods and services:** This help in increasing the standard of living of people, and helps to protect the consumer from exploitation by greedy businessmen.
- **Takeover of Sick units:** Closure of sick units may result in loss of employment to a large number of people and wastage of national resources, Public Enterprises like National Textile Corporation was set up to nationalize such units and to make them healthy and profitable.
- **Development of Agriculture sector:** It can be done if Public sector manufactures the fertilizers, pesticides, insecticides and useful machines. Or through the various research Public sector can improve the productivity by preventing crop disease etc.

## ROLE PLAYED BY THE PUBLIC SECTOR ENTERPRISES

- **Development of Infrastructure and Heavy Industries:** Industrial development of a country necessitates the foundation of an infrastructure base.The private sector neither has the zeal nor the capacity to invest in such infrastructural programmes. From this point of view, the public sector has a magnificent record. The State has successfully implemented various schemes of multi-purpose river projects,, hydroelectric projects, transport and communication, atomic power,steel, etc.
- **Maximizing the rate of economic growth :**Originally, the activity of the public sector enterprises was to be limited to a definite field of basic and key industries of strategic importance. There were certain fields where the private enterprise was shy to operate as they involved huge investment or risk. It was the public sector alone which could build the economic overheads such as power, transport, etc. Since then the ideological objective of capturing the "commanding heights" by the public-vector bas been duly fulfilled, it succeeded in creating the necessary infrastructural base for sustained industrial growth. It has tremendously boosted the technological capabilities.
- **Balanced regional development :** In the pre-independence period a major problem was regional economic disparities. There were certain areas where there was a heavy concentration of industrial activity. On the other hand, there were certain backward areas which went without industries. Industrial development was highly lopsided. Thus Maharashtra, West Bengal, Gujarat and Tamil Nadu, etc., were highly developed industrially. States like Orissa, Assam, Bihar, Madhya Pradesh etc. were highly backward. Besides, industries used to be gravitated towards the metropolitan areas, rather than the smaller towns. But imbalanced economic development is as bad as underdevelopment.
- **Strong Industrial base:**The contribution of industrial sector i.e., manufacturing, construction, electricity in GDP at Factor Cost has raised slowly and steadily during the plan periods. It was only 13.3 percent in 1950-51 to 21.6 percent in 1980-81 and further to 24.5 percent in 2 003-04. However, the contribution of agriculture in GDP at Factor Cost declined from 59.2 percent from 1950-51 to 41.8 percent in 1980-81 to 24 percent in 2003-04. Hence, industrial base is more better in now, in compare to what was in 1950-51. During the plan period, most of the industries like iron-steel, heavy engineering, coal, heavy electrical machinery, petroleum and natural gas chemicals and drugs, fertilizers and defence have increased remarkably.
- **Increasing employment opportunities :** The growth of the public sector has led to the expression of gainful employment opportunities. In addition to the primary effect of the public sector in creating employment opportunities, public sector investments also have

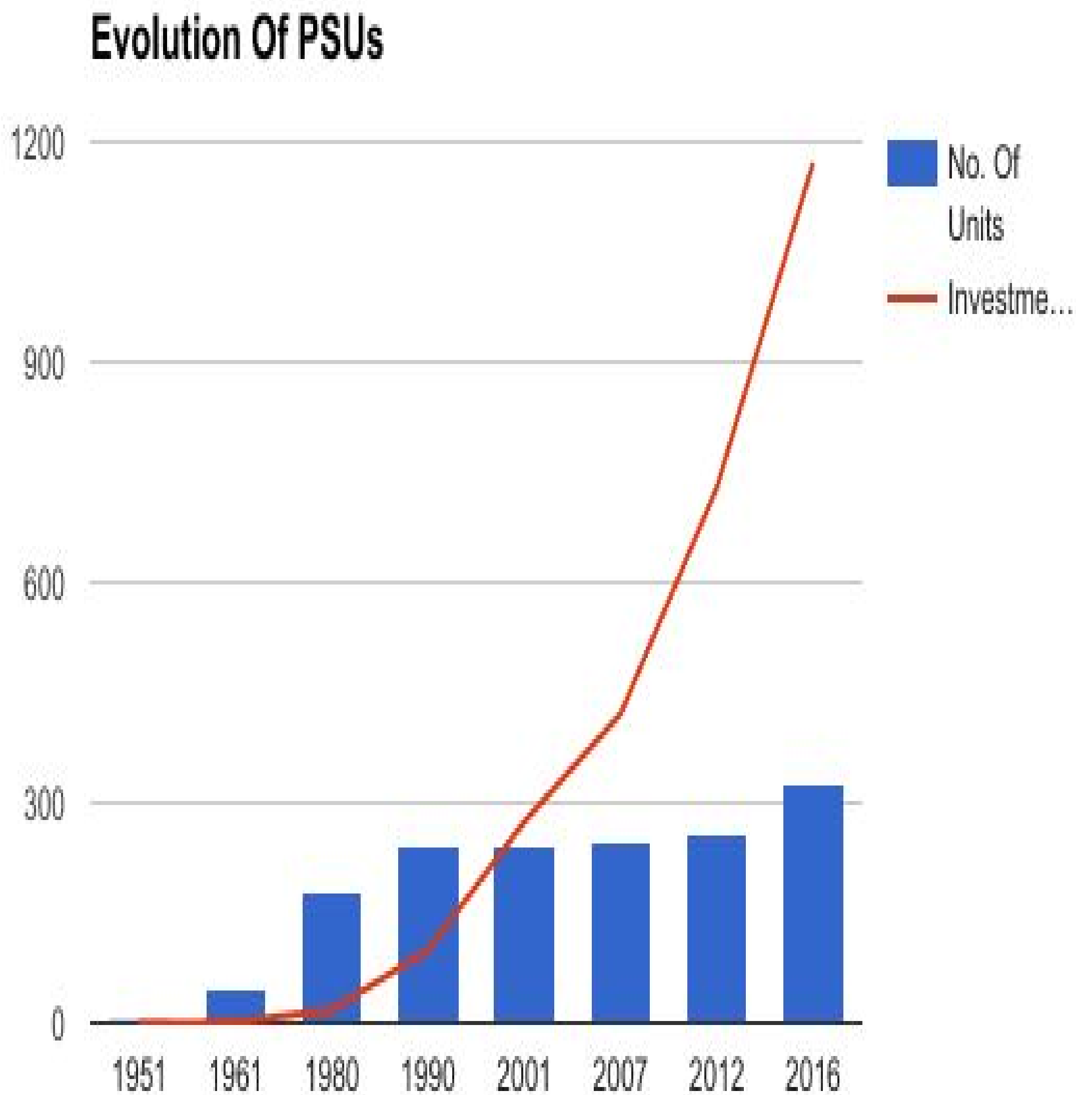
a multiplier effect on other sectors of the economy. This has a beneficial effect on the total employment position. In 1963-61, the number of people employed in public enterprises was only 1.82 lakhs. This figure rose to 14.08 lakhs in 1974 75 involving an increase of 671 per cent. Similarly the total amount of salaries and wages increased from Rs. 40’91 crores to Rs. 1,053 35 crores, involving an increase of 2,474.8 per cent, during the same period, In 1986-87 the number of working population in these industries stood at 22 lakhs.

- **Preventing concentration of economic power :** Preventing private monopolies and concentration of economic power is the avowed objective of our economic policy. Nationalization is considered as an antidote for the concentration of economic power in private hands. In India the public sector enterprises have grown both in number and in strength. Today, the public sector not only occupies the commanding heights in the economy, it has also penetrated into the production of essential consumer goods. The share of the public sector in the overall industrial production, has substantially gone up. This has effectively curbed the concentration of economic power. It has created a countervailing force against the growth of larger industrial houses.
- **Export promotion :**The public sector enterprises are substantially contributing to the country’s export earnings. The public sector has-built up a reputation abroad in selling plants, heavy equipment, machine-tools and other industrial products. She has created a goodwill in the third world countries-for her consultancy services and technical know-how. Public sector exports also include consumer goods. The role of the State Trading Corporation, or the Minerals and Metals Trading Corporation has been quite creditable in promoting exports. Between 1968-69′ and 1984-85, the percentage share of public sector enterprises in India’s export trade went up from 20.05 to 38.1 per cent. Public sector exports increased from Rs. 272 crores in 1968-69 to Rs. 4,522 crores in 1984-85. In 1976-77 the public enterprises earned Rs. 2,248 crores in foreign exchange. The public enterprises thus had a splendid performance.
- **Import substitution :**The public sector enterprises have also-succeeded in their efforts in import substitution. Today many commodities starting from basic drugs to highly advanced equipments are manufactured in the public sector, which previously used to be imported from abroad. In certain fields public enterprises were specially started to reduce imports from abroad, and achieve self-sufficiency. Public enterprises like Hindustan Antibiotics Ltd. or Bharat Electronics Ltd. or Hindustan Machine Tools etc., have done a remarkable job in import substitution. This has resulted in saving of precious foreign exchange. Today there is a special drive in the public enterprises to utilize indigenous materials and domestic skill.

## REASONS FOR THE ECONOMIC REFORMS

The most important criticism levied against the public sector has been that, in relation to the capital employed, the level of profits has been too low. Even the government has criticised the public sector enterprises on this count. For instance, the Eighth Five Year Plan notes that the public sector has been unable to generate adequate resources for sustaining the growth process.

- **Price Policy of Public Enterprises:** The purposes of setting up and operating public sector enterprises are varied and price policy is determined by the objectives which they are expected to serve. Even under conditions of monopoly, the objective of the pricing policy of a particular public sector enterprise may not be profit maximisation. Indian Railways, Indian Airlines Corporation, State Electricity Boards are examples of public monopolies. Public enterprises like Steel Authority of India and the Fertilizer Corporation of India also operate in seller's market. It is very easy for these enterprises to earn huge profits simply by increasing their prices. But since their object was not profit maximisation but fulfilment of some social objective, they opted for losses in some cases while in some instances they just tried to equate total revenues to total costs.
- **Under-utilization of Capacity:** Under-utilization of installed capacity is another reason for the low level of profitability in public sector enterprises. A large number of these enterprises have operated at less than 50 per cent of their capacity for a number of years. The public sector enterprises —became increasingly instruments for meeting immediate or ad hoc demands such as producing mass consumption goods, stimulating growth in economically backward areas or using locally available raw materials. Others are inefficient operation and poor management of some enterprises, political interference in day-to-day working, labour disputes etc.
- **Excessive Political Interference:** There existed considerable political interference in the operational aspects of PSEs in terms of appointment in the management, pricing of products, location of projects. The decisions were guided by political considerations and not by economic factors.This lead to a large amount of inefficiency in the working of PSEs.
- **Delays in Decision-Making:** The red-tapism and bureaucratic management caused delay in decision-making of these organizations. PSEs thus failed to take advantage of opportunities thrown open by the market.Important decisions were delayed which lead to further more decrease in efficiency.
- **Lack of Accountability:** The appraisal system lack performance-based remuneration system. The system lacks incentives to improve and penalties for delays and failures. The security of service makes them lethargic and reduces creativity.




**Source:-**
**http://www.dpe.gov.in/pesurveyreports/public-enterprises-survey-2015-16**

# REFORMS

The new industrial policy announced by the government in July 1991 emphasised the following four major measures to ‗reform‘ the public sector enterprises: (i) reduction in the number of industries reserved for the public sector from 17 to 8 (reduced still further to 3 later on) and the introduction of selective competition in the reserved area; (ii) the disinvestment of shares of a select set of public sector enterprises in order to raise resources and to encourage wider participation of general public and workers in the ownership of public sector enterprises; (iii) the policy towards sick public sector enterprises to be the same as that for the private sector; and (iv) an improvement of performance through an MOU (memorandum of understanding) system by which managements are to be granted greater autonomy but held accountable for specific results.

**Disinvestment:**
The term “Disinvestment” is the opposite of the term “Investment”.Disinvestment refers to the action of an organization the government in selling or liquidating an asset or subsidiary. It is also referred to as ‘divestment’ or ‘divestiture.’ In simple words, disinvestment is the withdrawal of capital from a country or corporation.

**Disinvestment Policy:**
For the first four decades after Independence, the country was pursuing a path of development in which the public sector was expected to be the engine of growth. However, the public sector overgrown itself and its shortcomings started manifesting in low capacity utilisation and low efficiency due to over manning, low work ethics, over capitalisation due to substantial time and cost overruns, inability to innovate, take quick and timely decisions, large interference in decision making process etc. Hence, a decision was taken in 1991 to follow the path of Disinvestment.

**Objectives of Disinvestment:**
Following objectives were stated in July, 1991 while propounding the disinvestment policy:

- To meet the budgetary needs.
- To improve overall economic efficiency.
- To reduce fiscal deficit.
- To diversify the ownership of PSU for enhancing efficiency of individual enterprise.
- To raise funds for technological up gradation, modernization and expansion of PSUs.
- To reduce the financial burden on the Government.
- To improve public finances.
- To introduce, competition and market discipline.

- To encourage wider share of ownership.

**Period from 2001-02 to 2003-04**

This was the period when maximum number of disinvestments took place. These took the shape of either strategic sales (involving an effective transfer of control and management to a private entity) or an offer for sale to the public, with the government still retaining control of the management. Some of the companies which witnessed a strategic sale included:

- BHARAT ALUMINIUM CO.LTD.(BALCO)
- CMC LTD.
- HINDUSTAN ZINC LTD.
- HOTEL CORP.OF INDIA LTD. (3 PROPERTIES: CENTAUR HOTEL,JUHU BEACH, CENTAUR HOTEL AIRPORT,MUMBAI & INDO HOKKE HOTELS LTD.,RAJGIR)
- HTL LTD.
- IBP CO.LTD.
- INDIA TOURISM DEVELOPMENT CORP.LTD.(18 HOTEL PROPERTIES)
- INDIAN PETROCHEMICALS CORP.LTD.
- LAGAN JUTE MACHINERY CO.LTD.
- MARUTI SUZUKI INDIA LTD.
- MODERN FOOD INDUSTRIES (INDIA) LTD.
- PARADEEP PHOSPHATES LTD.
- TATA COMMUNICATIONS LTD.

The valuations realized by this route were found to be substantially higher than those from minority stake sales.
During this period, against an aggregate target of Rs. 38,500 crore to be raised from PSU disinvestment, the Government managed to raise Rs. 21,163.68 crore.
According to the BUDGET 2016-17, Disinvestment target of Rs.72.5 thousand crores is set .
Three Railway PSU are set to be listed:-
IRCTC,IRCON,IRFC.

**De-Reservations:**

The 1956 Industrial Policy Resolution had reserved 17 industries for the public sector. The 1991 industrial policy reduced this number to 8: (1) arms and ammunition, (2) atomic energy, (3) coal and lignite, (4) mineral oils, (5) mining of iron ore, manganese ore, chrome ore, gypsum, sulphur, gold and diamond, (6) mining of copper, lead, zinc, tin, molybdenum and wolfram, (7) minerals specified in the schedule to the atomic energy (control of production and use order), 1953, and (8) rail transport. In. 1993, items 5 and 6 were deleted from the reserved list. In-199899, items 3 and 4 were also taken out from the reserved list. On May 9, 2001, the government opened up arms and ammunition sector also to the private sector Thus, now only 3 industries are reserved exclusively for the public sector. These are atomic energy, minerals specified in the schedule to the atomic energy (control of production and use order) 1953, and rail transport. The new industrial policy of 1991 threw open all these industries for the private sector for investment and growth. Thus the new policy indicates the Government’s intention to invite a greater degree of participation by the private sector in important areas of the economy.

**Classification:**

Various PSUs have been awarded additional financial autonomy. These companies are "public sector companies that have comparative advantages", giving them greater autonomy to compete in the global market so as to "support  in their drive to become global giants".Financial autonomy was initially awarded to nine PSUs as *Navratna* status in 1997.In 2010, the government established the higher *Maharatna* category.

**MAHARATNA:**

The six criteria for eligibility as Maharatna are:
(1) Having Navratna status.
(2) Listed on Indian stock exchange with minimum prescribed public shareholding under SEBI regulations.
(3) An average annual turnover of more than Rs. 20,000.crores during the last 3 years. Earlier it was Rs 25,000 Crore. An average annual net worth of more than Rs. 10,000 crore during the last 3 years. Earlier it was Rs. 15,000 crore.
(4) An average annual net profit after tax of more than Rs. 2500 crore during the last 3 years. Earlier it was Rs. 5000 crore.
(5) Should have significant global presence/international operations. An average annual net profit after tax of more than Rs. 2500 crore during the last 3 years. Earlier it was Rs. 5000 crore.
(6) Should have significant global presence/international operations.
List of Maharatna:

- Bharat Heavy Electricals Limited.
- Coal India Limited.
- GAIL (India) Limited.
- Indian Oil Corporation Limited.
- NTPC Limited.
- Oil & Natural Gas Corporation Limited.
- Steel Authority of India Limited.

**NAVRATNA:**

Criteria for Navaratna's:
(1) A score of 60 (out of 100), based on six parameters which include net profit, net worth, total manpower cost, total cost of production, cost of
services, PBDIT ,capital employed.
(2) A company must first be a Miniratna and have 4 independent directors on its board before it can be made a Navratna.

(3) Allows to raise up to Rs. 1,000 crore or 15% of their net worth on a single project or 30% of their net worth in the whole year.
List of Navratna's:

- Bharat Electronics Limited
- Bharat Petroleum Corporation Limited
- Container Corporation of India Limited
- Engineers India Limited
- Hindustan Aeronautics Limited etc.

**MINIRATNA:**
Criteria for Miniratna
It also divided into two parts:
(i) Miniratna-I: up to Rs. 500 crore or equal to their net worth, whichever is lower.
(ii) Miniratna-II: up to Rs. 300 crore or up to 50% of their net worth, whichever is lower. Have made profits for the last three years continuously and should have a positive net worth.
List of Miniratna:

- Airport Authority of India Limited
- BEML Limited
- Bharat Sanchar Nigam Limited
- IRCON International Limited etc.

**Memorandum Of Understanding :**
One of the major initiatives towards the public sector as outlined in the new industrial policy of July 1991 was to bring all public sector enterprises under the system of Memorandum of Understanding (MOU). The system of MOU envisages an arm's length relationship between the PSU and the administrative ministries. It gives clear targets to PSUs and ensures operational autonomy to them for achieving those targets. The MOU system was started in 1987-88 with four PSUs signing MOUs. This number went up to 144 CPSEs in 2008-09. The government has now decided that all CPSEs including risk and loss-making and CPSEs under construction will be covered under the MOU system.MoU system involves goal setting in financial and nonfinancial areas and performance evaluation of these goals.
The MoU negotiations meetings are attended by the Chief Executives of the CPSEs, Senior Officers from the administrative Ministries and the representatives of the nodal Government agencies such as Niti Aayog and Ministry of Statistics & Programme implementation.

## CHALLENGES

- **Multiple Principles:** Most Central PSUs these days are being plagued by multiple principles and multiple goals often resulting in conflicting situations for these enterprises. The outcome of these conflicting principles and goals lead to the public sector enterprises being unable to ascertain the outcome. Conflicting goals often result in affecting overall performance of the organization.
- **Broad based decision making structures:** More often than not, the decision making structures in Central PSUs are broad based, resulting in people working at cross purposes owing to lack of proper coordination and a common objective. The principle of profit maximization takes a backseat while vested interests seem to take over.
- **Problem of untapped talent:** PSUs were established with the purpose of absorbing surplus labour while reducing unemployment rates in the country. However, owing to stringent recruitment practices that are filled with old-school thoughts and political interventions, these enterprises lost their sheen compared with their private counterparts who despite lacking size and might of such enterprises, end up in moving ahead in recruiting the country's best minds. Moreover, lack of transparency in the entire recruitment process stops students from top educational institutes from applying for these government posts.
- **Private sectors steer ahead in terms of compensation structure:** On the back of economic liberalization and movement of compensation structures from socialist regimes, the differentials between the public sector and their corporate counterparts is widening. If this disparity is not controlled, the private sector will continue to draw all the talent and public sector enterprise would be left high and dry. Despite the sixth pay commission being implemented, there is still not enough parity between the compensation structures prevalent in the public sector and their private sector counterparts.
- **Inadequate implementation of quantitative performance metrics:** Performance measurement of the past years, such as linking financial parameters with operational efficiency led to deterioration of liability. As a result, public sector enterprises find it difficult to compete with private sector companies, whose processes are better aligned. Owing to this, the opportunities available to this sector have become constricted.
- **Lack of autonomy in decision making:** Public sector enterprises have always suffered due to lack of autonomy. Initially, delegation of powers was restricted. Consequently, when the Indian economy opened up in the early nineties, such companies were caught off-guard and lost out on several opportunities of expansion both within the country as well as overseas. The need of the hour was to divest more by granting more financial

and operational autonomy to the top management in decision making. Creating Maharatnas and Navratnas was one such step towards creating greater autonomy.

## CONCLUSION

- The public sector is an integral part of the Indian economy and a key growth driver. With the advent of globalization, the public sector gained credence in the face of faced new challenges in developed economies. This sector provided the required thrust to the economy and developed and nurtured human resources, the vital ingredient for the success of any enterprise.
- As we know the economic environment is changing day by day, so any policies or rules cannot be said to be fruitful forever. For some time it may be good for the economy but it has to be amended one day or the other. So we can say that the change in the role of public sector enterprises can be good as well as bad when seen from all point of views.
- The change in role has two effects -positive as well as negative. Positive effect can be the increase in the efficiency of the industries due to the involvement of private sector, thus increasing the competition in the market, inclusion of better technology, improvement in quality of the product, increase in the accountability to the public, increase in the investments leading to more and more new projects for the betterment of the society.
- The negative effect can be  change from government controlled economy to the market driven economy. Initially the economy was government controlled as all the power was in the government's hands, so it was predictive and it did not lead to much major losses, as it was under control. But later it has turned to market driven due to the privatization, now it is not predictive and cannot be fully controlled by government, it has many dangers.One of the example is Great Depression of 2008.

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