Disinvestment Kinetics

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Abstract: ***Disinvestment Kinetics deals with the country's disinvestment past, present and future in the public sector enterprises. Government's policy of disinvestment has been analyzed over the period since its inception in 1991. Observational study of current public sector enterprises like Bharat Petroleum Corporation Limited and Life Insurance Corporation has been done.***

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Disinvestment is the process of selling an asset by the government or any other organization. Disinvestment in public sector enterprise is done by the government either by selling stakes or listing the enterprise on stock exchange for public issues. Disinvestment's prime target is to reduce the monetary load on the government due to inefficacious PSUs and to improve the finance. It encourages private players to enter the specific sector and infuse private capital. Privatization introduces competition and market discipline which ensures better allocation of equity and debt of the enterprise.

Disinvestment, the last resort weapon, and instrument in the hands of the Government of India has enabled the public sector to become more efficient and responsible as well as accountable to the public. In 1991, the PSUs of India faced problems like low-productivity, over-manning and increasing fiscal deficit which led to the adoption of this new approach towards the public sector.

In 1991 the Chandrashekar Government targeted to divest up to 20% of the government equity in the PSEs in the favor of institutional investors, mutual funds and financial institutions in the public sector. It was done to broaden the base of equity management, enhance the availability of resources for the enterprises and yield Rs 2500 crores to the exchequer.

In 1993 the Government of India set up a committee under the chairmanship of the former RBI Governor C. Rangarajan, in 1993. Rangarajan Committee produced a report in April 1993 and recommended the percentage of equity shares for disinvestment should be below 49 percent in the industry reserved for the public sector and more than 74% in other industries. The Committee recommended 4 methods of disinvestment, namely-

1) Trade Sale
2) Strategic Sale
3) Offer of shares
4) Closure of Assets

The sale proceeds from the divested enterprises will be channelized into the National Investment Fund to be maintained separately from the Consolidated Fund of India. 75% of the annual income of the fund will go to finance the social schemes, which will uplift the healthcare, employment, and education system of the country. The rest 25% will be used to revive the PSUs that can produce returns and in order to increase their capital base to finance expansion or diversification.

In 1996 the Ministry of Industry constituted a Public Sector Disinvestment Commission for a period of 3 years under Shri G.V. Ramakrishna along with four other members. The Commission submitted reports on 58 PSEs. Ministry of Disinvestment reconstituted the commission in 2001 under Dr. R.H. Patil as Chairman along with 4 other members. The commission submitted reports on 41 PSEs, out of which 4 PSEs (NCL, MOIL, RITES, and PEC) were review cases of recommendations of the earlier commission. In 20 cases the commission itself did not recommend strategic sale. In 6 cases, the Commission had recommended an offer for sale of minority shares. In 12 cases, the Government decided not to pursue Strategic Sales/disinvestment out of which 3 cases; the reason was that bidders were not found for these companies. In 11 cases, strategic sales were implemented out of which 2 cases, privatization has been partly implemented. The numbers indicate failure of Government at the process as the real figure of Rs 20000 crore was far less than the target of Rs 55000 crore between 1992 and 2001.

The liquidity trapped Government has again announced the tool of disinvestment for its survival in the current financial years. Disinvestment target for FY 21 is at 2.1 trillion rupees nearly double its current fiscal target. Ministry of Finance is expecting to raise this sum in the proportion of 90000 crore from an IPO of LIC and the rest by a stake sale in IDBI. This aggressive disinvestment is against the backdrop of declining tax collections and a sharp decline in the economy that the government is attempting to revive.

Few economists and industry experts fear this decision by citing the example of privatization of American schools which has demeaned the right to education because of a sharp rise in their fees. Disinvestment of the United Kingdom's Railways in 1994 was a fateful decision as the franchisee model didn't fulfill the objectives.

Department of Investment and Public Asset Management announced Bharat Petroleum Corporation Limited to be divested by stake sale. The Government has an ownership of 52.98% valued at 48700 crore in the oil giant. BPCL accounts for 25% of the oil sector of India and refines around 13% of crude oil i.e. 38.3 million metric tons. According to the data available with the Petroleum Planning and Analysis Cell, BPCL has nearly 15,000 fuel retail outlets, 6000 LPG distributors and 58 aviation turbine fuel stations across the country. Government firms are not eligible to bid for the proposed transaction and only the private players with a net worth of over $10 billion are eligible to bid.

Cut in crude oil prices by state-run Saudi Arabian Oil Company, is one of the prime reason behind the rising stock of BPCL. Therefore, this will improve the finances and ratios of the company which will benefit the investors in the long term. Since the Government has announced the entire stake sale, the new buyer would have full control of the business.

The state-run insurance giant, Life Insurance Corporation has net assets of more than Rs 31 lakh crores and is way bigger than RIL in terms of market capitalization. LIC employs 1,11,979 peoples and has a net profit at Rs 2.6 lakh crores annually that is close to 10% size of overall government expenditure. LIC even earned significant income from the dividend of Rs 1.76 lakh crore. LIC offers a sovereign guarantee to the policyholder and holds 75.6% of the market share in the insurance sector.

Government plans to divest 10% of LIC through IPO and expects to raise nearly 80000 crores, which is very critical for the current year's target. The only problem with the process is that there is no provision of a public offer in the LIC Act of 1956. Therefore the law needs to be amended before any further step can be taken in the process.

LIC's listing would unlock the value of insurer and would provide an opportunity for retail investors to participate. This step would enhance transparency as it has to disclose investment and loan portfolios more frequently.

To ensure equity in the process, a third-party valuation of the assets and a minimum number of bidders should be necessary pre-conditions to going ahead with each sale. The Government should ensure that the strategic sale is transparent and a minimum reserve price of the assets being auctioned off is decided. In the end, the Government should direct the divestment proceeds into the professionally managed National Investment and Infrastructure Fund so that the funds instead of frittering away in salary payouts are used prudently in infrastructure assets that yield enduring returns to the economy.